War Finance Primer

National Bank of Commerce
in New York

MAY, 1917

A BIG loan helps to ensure victory. A big loan will also shorten the War. It will help to save life; it will help to save the British Empire; it will help to save Europe; it will help to save civilization.

The Prime Minister of England,
Guildhall, January 11, 1917.

War Finance Primer

THE greatest immediate service the American people can render in this war for universal liberty throughout the world is to furnish the means for its vigorous prosecution. This bond issue is the first step. I earnestly bespeak the co-operation of every citizen throughout the length and breadth of the land in this great service of patriotism.

The Secretary of the Treasury,
Washington, May 2, 1917.

Service Department

National Bank of Commerce in New York

May, 1917

Summary

In the following pages three main sections are offered. The first was prepared by Professor E. R. A. Seligman of Columbia University, one of the world's foremost authorities on Public Finance. He surveys the present American situation with regard to the possible sources of taxation, and outlines what he believes to be the proper balance between taxation and bond issues.

The second section is a chapter on "The Financial Management of a War" from the standard work by Dr. Henry C. Adams, entitled "Public Debts." This chapter is recognized generally as the best study in English on the subject. The book is now out of print, but we are able, through the courtesy of the author and the publishers, Messrs. D. Appleton and Company, to make it available at this time. It was reprinted at the time of the Spanish War and the copyright has only recently been renewed.

The third section contains a brief study of financing and taxation during the present war, together with figures on national wealth. Messrs. R. R. McElvare and Louis Gottlieb of Columbia University under the direction of Professor Seligman, prepared this material for us from official documents. Owing to unsettled conditions reliable material of this sort is extremely hard to accumulate.

This book has been sent to members of Congress, to all national and state banks and trust companies, to prominent business men and to representative newspapers. It is believed it will be an aid to clear thinking on the fundamentals of war financing and will tend to bring the country solidly behind the financial program of the Government. Readers of this book who care to pursue the subject further are invited to communicate with the National Bank of Commerce in New York.

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Foreword

This book is published by the National Bank of Commerce in New York as part of its effort to co-operate with the Government in war financing.

Economic forces have turned the tide of many battles. United States dollars as well as United States men must be sent to the front. Whenever our country's financial resources are mobilized and utilized, they will have a profound effect upon the immediate prosecution of the war, and, if well used, upon the economic stability of our country in future generations.

War finance problems are not simple, but the main principles involved may be outlined with some degree of certainty. After having made a survey of the available material, we believe this War Finance Primer will help to point out the dangers involved and the best general course to be adopted.

The crux of the matter is to strike a balance between loans and taxes. The present generation cannot avoid economic sacrifice. At the same time our industrial and commercial life should be fostered and the incentive to do business should be preserved. To some extent we must pay as we go; but we must not kill the goose that lays the golden egg.

Our economic stability demands that we determine the happy medium between bond issues and taxation. The present problem is not only to raise the necessary money for a vigorous prosecution of the war, but to impress upon Americans, probably the most extravagant people in the world today, the fact that thrift and economy are the only permanent basis of a nation's commercial greatness.

The Government has wisely indicated its intention to avail of the country's financial and commercial skill. The

financial world has unreservedly offered its facilities without profit. The banks will do their part in raising the money needed by the Government.

This situation provides a wonderful opportunity to educate the people to co-operate with the Government in financial matters. In France, the securities of the French Government are the favorite form of investment. Herein lies one of the reasons for French financial and commercial soundness. The great commercial expansion to follow the present war will rest upon a sounder and more permanent footing if the American people can be induced to participate more fully in the securities of our Government and of our allies.

JAMES S. ALEXANDER,
President.

May, 1917.

PART I.

British War Loan Advertisements

THESE British war loan advertisements are reproduced from THE LONDON TIMES. The issue in which each appeared is indicated below the reproduction. Each of them except the last two occupied a full page.

HAVE YOU INVESTED *in* THE WAR LOAN?

THE LAST DAY IS FRIDAY THE 16TH AND GERMANY IS WATCHING US.

IF YOU HAVE NOT ALREADY INVESTED EVERY SHILLING YOU CAN SCRAPE TOGETHER——DO SO NOW.

If you have £5 or any amount up to £50 to lend, go to the nearest Money Order Post Office, and they will invest it for you in War Loan. You will get a receipt for your money and afterwards they will send you your stock.

HAS IT OCCURRED TO YOU that you can help to end the War by borrowing on your Life Policy

OR

by obtaining a Loan from your Bank

OR

If you have £50 or over to lend to your Country, go to your Bank Manager. He will help you to increase your lending power. The Bank Managers have intimated their desire to do everything in their power to make the Victory Loan an overwhelming success

By CONVERTING YOUR TREASURY BILLS INTO WAR LOAN.

The Bank will accept the War Loan it buys for you as security for what it lends to you.

FEBRUARY 5, 1917.

"WHOEVER has taken no share at all in the Nation's War Loan when Friday arrives can only be regarded as hopelessly *déclassé,* and equally hopelessly stupid. For not merely is this War Loan the most important ever launched in our financial history by a British Government on account of its objects, but it is also the most attractive in its terms as an investment. And no secret has been made of the fact that such terms will not be repeated. Those who keep their money in their pockets now will assuredly be sorry for it later, when they are asked to show how they responded to the call of the State."

"THE TIMES."

WHAT CASH OR BANK BALANCE HAVE YOU? WHAT SECURITIES OR PROPERTIES CAN YOU BORROW AGAINST? HOW MUCH CAN YOU SAVE THIS YEAR? BY WHICH OR ALL OF THESE METHODS ARE YOU GOING TO INCREASE YOUR WAR LOAN INVESTMENT?

THE Victory War Loan ***must*** be an overwhelming success, and there remain only three days in which you can do ***your*** part. Realise your individual responsibility.

LEND to the Government every shilling you can scrape together. Decide to wear old clothes, old boots, old dre ses; eat, drink and smoke less, and then borrow against your future savings to invest in

THE WAR LOAN.

GO TO-DAY TO YOUR BANK, Employer, or Local War Savings Committee, and arrange for an advance, and then buy War Loan through any Money Order Post Office, Bank or Stockbroker.

YOUR MONEY IS SAFE. Your interest is sure, and whenever you need your money you can sell your stock through any Bank, Stockbroker, or Post Office. Do your duty to-day—there is still time.

— at 12 o'clock to-day
STOP
and ask yourself this question
Have I helped the War Loan?

HAVE you done everything in your power to make the Victory War Loan an overwhelming success? If you have, your conscience is clear.

IF you have not done everything in your power do so *now* at the Post Office, Bank, or through your Stock Broker. There is still time.

YOUR COUNTRYMEN ARE *GIVING* THEIR LIVES

YOU ARE ONLY ASKED TO *LEND* YOUR MONEY

To-morrow is the Last Day to invest in

THE WAR LOAN

FEBRUARY 15, 1917

FEBRUARY 5, 1917.

THE WAR LOAN and the Y.M.C.A.
Will you help to turn the Scale?
His Majesty The King
The Premier (Mr. Lloyd George)
Lord Derby
Comfort
Recreation
Efficiency
Morale
Victory
VICTORY
£100,000
Only Three Days more
TO assist in the great National effort to make the new War Loan an overwhelming success, every penny subscribed to the Y.M.C.A. during the present week, to February 16th (unless specially earmarked for other purposes) will be used for purchasing War Loan Stock.
MORALE
COMFORT
EFFICIENCY
RECREATION
£50,000
Facts that Weigh
400,000 Soldiers and Sailors slept in the London Y.M.C.A. Hostels last year.
£600,000 have been spent on Y.M.C.A. Huts, Tents and Equipment. Every day brings urgent appeals for additional Huts.
160,000 cups of hot cocoa were given free in November, in one army area alone.
£60,000 per annum is being spent on free Stationery, which enables the men to keep touch with home.
200 to 250 Relatives of dangerously wounded men are guests of the Y.M.C.A. in France each day.
£500, £750, or £1,000 given to-day for War Loan, will enable the Y.M.C.A. to erect another much-needed Hut.
To give now is to render a double service to your Country
at the most critical time in her great history. SEND YOUR GIFT TO-DAY to the Hon. Treasurer, Y.M.C.A. National Headquarters, 12-13, Russell Square, London, W.C.
WILL YOU POST THIS TO-DAY?
Name
Address

HAVE you asked the Bank Manager how he can help you to subscribe to the War Loan?

If not—
do so to-day.

The more you lend—
the sooner the war will end.

ANY Money Order Post Office will hand you a £1 War Savings Certificate for 15/6. Any Bank will buy War Loan for you from £5 upwards. Or go to your local War Savings Committee, who will do everything for you.

YOUR

MONEY
CANNOT
BE
NEUTRAL

HAVE you helped your Country by investing in the War Loan, or have you helped Germany by keeping your money in your pocket?

THE
WAR LOAN
CLOSES
TO-NIGHT.

PART II.

How to Finance the War

How to Finance the War*

By E. R. A. SELIGMAN
McVickar Professor of Political Economy, Columbia University
and
ROBERT MURRAY HAIG
Assistant Professor of Economics, Columbia University

Making war is easily the most expensive function of government. Always costly, in modern times it has come to involve truly astounding expenditures. When, as is now the case, the entire accumulated wealth and productive power of a nation join with its man power to match strength with the adversary, the skill used in raising the necessary funds is of paramount importance. Having decided to enter the conflict, the United States government stands in immediate need of billions of dollars. How many billions will be required before the war is brought to its end cannot be foretold; but our resources may be strained to their capacity. **A number of plans have been proposed for meeting the situation, each different in its fiscal and economic consequences. The problem is to determine upon the particular program which will best distribute the burden in accordance with ability to bear it, and which will produce the huge sums needed with the least impairment of our resources.** To cripple ourselves at the outset of the war with a faulty financial plan might have disastrous consequences. To adopt any but the wisest policy of finance would involve unnecessary waste and suffering.

New Policies Are Called For

There are good reasons why the best plan for financing this particular war differs radically from the plans which we have used in the past. Political problems, for example, which in other days have been powerful factors

* COLUMBIA WAR PAPERS: This article was prepared by Professor Seligman for publication as one of the valuable Columbia War Papers, a series of pamphlets on the problems and duties of American citizens in meeting the national needs in the present world conflict. By arrangement with the Division

in moulding fiscal policies are fortunately of negligible importance. Moreover, the economic situation is infinitely more favorable than any which has existed heretofore. We have not only greater resources, but resources of a different type upon which to draw. In other wars, our traditional policy has usually been to tax ourselves only when no one would lend us the money. In the absence of political and economic exigencies, a very different policy may be adopted. Finally there have been radical social changes since our previous wars which will affect our methods of finance. Types of taxes and forms of bond issues which were considered unobjectionable not long ago will not now measure up to the ideas of justice established by a democracy which has become progressively more enlightened and intelligent.

The problem of financing the war resolves itself into three distinct parts, each of which will be treated in a separate section. The first is concerned with the general question of loans versus taxes. To what extent shall the expenses of the war be met by borrowed money and to what extent by the proceeds from taxation? The second section discusses the kind of indebtedness to be incurred and the third the methods of taxation to be employed.

We Must Prepare for a Long War

But before these problems can be discussed with any degree of definiteness, it is necessary to make some

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of Intelligence and Publicity of the University, the material is published simultaneously by the National Bank of Commerce in New York for general circulation among bankers and business men. The article is copyrighted by Columbia University.

A complete list of the Columbia War Papers, copies of which may be had upon application to the University, follows:

No. 1, ENLISTMENT FOR THE FARM, By John Dewey; No. 2, GERMAN SUBJECTS WITHIN OUR GATES, By the National Committee on Prisons and Prison Labor; No. 3, MOBILIZE THE COUNTRY-HOME GARDEN, By Roscoe C. E. Brown; No. 4, OUR HEADLINE POLICY, By Henry Bedinger Mitchell; No. 5, DEUTSCHE REICHSANGEHÖRIGE HIER ZU LANDE, Vom Nationalausschuss für Gefängnisse und Gefängnisarbeit; No. 6, FOOD PREPAREDNESS, By H. R. Seager and R. E. Chaddock; No. 7, HOW TO FINANCE THE WAR, By Edwin R. A. Seligman and Robert Murray Haig; No. 8, FARMERS AND SPECULATORS, By B. M. Anderson, Jr.; No. 9, A DIRECTORY OF SERVICE, Compiled under the direction of John J. Coss; No. 10, CITY GARDENS, By Henry Griscom Parsons; No. 11, BREAD BULLETS, By R. S. MacElwee; No. 12, RURAL EDUCATION IN WAR, By Warren H. Wilson.

general assumptions regarding the probable length of the war and the part we are to play in it. For the magnitude of the sums to be raised is of very great importance in connection with the probable strain on the revenue system because of increased taxation, and in connection with the general economic effects of an appeal to credit.

There is every indication that the policy of the United States in this war will be one of enthusiastic cooperation with the Allies. To the extent that we are at present prepared to furnish military assistance, that will be given; far-reaching measures will be adopted to train a large army; and economic aid will be extended. But there appears to be a wide-spread belief that the war will end very quickly, perhaps before our power can be brought to bear to any considerable extent. If this view is correct, the financial problem will, of course, be insignificant. But it is the part of prudence to prepare for the alternative issue. In this, we may well learn a lesson from the other belligerents. Although Lord Kitchener did predict a three-year war, the fiscal policies of all the European nations were predicated on a much shorter period; and it was only after a lapse of a considerable time that plans for financing a protracted contest were adopted. Lord Kitchener's three-year period has almost expired and yet even now it cannot be definitely asserted that the end of the war is in sight. There appears to be no sound basis of known facts for the belief that the Central Powers are on the verge of collapse. What the true military and political situation may be in Germany, it is impossible to judge with accuracy. But he is an optimist indeed who would depend upon an economic or financial breakdown to bring about the cessation of hostilities within a short time.

Our War Cost May Reach Ten Billions a Year

Assuming that we are to enter into this war in a whole-hearted manner and assuming, as seems prudent and reasonable, that the war will last long enough for us to bring our forces into action, how much money will be needed? This question, of course, can be an-

swered only by the roughest of estimates. With no experience of our own to guide us, the English experience forms, perhaps, our best material for a guess. Bonar Law has recently stated that the total expenditures of England for the fiscal year just ended will be about £2,140,000,000 or approximately ten and one-half billions of dollars. It is not probable that our full share in the war will be less than this. Doubtless, our army at first will be considerably smaller than that of Great Britain; but it must be remembered that the cost of our military forces, particularly the pay of our soldiers and sailors, is larger than is the case abroad. Before the war, the military and naval expenditures of the United States, in spite of the insignificant size of the army, were approximately as great as those of Germany. An expeditionary force to Europe would involve outlays of enormous extent. Finally, we shall doubtless be immediately called upon to make considerable advances to the Allies. All in all, it would seem that our war expenses might reasonably be expected to approximate ten billions a year. How can this sum best be secured?

I. LOANS VERSUS TAXES

There is in this country no 'war chest' upon which to draw in an emergency; there are no profits from enterprises conducted by the government; and there will probably be no indemnities wrung from a conquered people. It follows that the money must be collected by taxation or be borrowed. It is barely conceivable that all the money might be borrowed and taxation avoided entirely for the present. On the other hand, it is being seriously urged by many well-informed persons that the entire cost of the war be met by current taxes. There are a number of reasons why the wisest course will lie between these extremes.

History Points Out What to Avoid

Our own history is perhaps most useful for the purpose of pointing out what to avoid rather than what to

adopt in war finance; but it is, nevertheless, of importance to recall that the policy of meeting all war expenses by taxation is entirely new in the United States. Indeed, the question here has rather been whether taxes could be made sufficiently high to meet merely the interest charges on the money borrowed without any allowance even for amortization. Thus, Gallatin's original war budget, at the time of the struggle with England, contemplated a tax levy for interest only. But the taxes actually imposed proved insufficient even for this purpose, with the result that in 1814 Dallas had to be summoned to extricate the country from a condition of bankruptcy—an end which he accomplished through a more vigorous policy of taxation. Again, the financial history of our Civil War is primarily one of loans, forced or voluntary, rather than one of taxes. During 1862 and 1863, when the proceeds from loans were about $300,000,000, the increase in taxes over those of peace times scarcely sufficed to pay the interest on the new debt. During the first year of the conflict, they were entirely inadequate for this purpose. It was not until after 1864 that the taxes made any substantial contribution to war expenses. Finally, in the Spanish war, a $200,000,000 loan was the foundation stone of the financial plan, the sole increases in taxation being new internal revenue duties which yielded only about $25,000,000 of additional revenue in 1898 and $125,000,000 in 1899.

Not only would it be a novelty to American finance to levy war taxes in larger amount than required for interest on the debt, but it would be almost as much a novelty in European countries. Germany, during the present war, refrained for a long time from imposing any war taxes at all, and the recent additions to the imperial tax budget are intended primarily to defray the interest on the huge loans. The policies of England and France have been essentially the same except that England began to tax for interest purposes somewhat earlier than the others. The total war expenditures of England up to April, 1917, have been stated by Mr. Bonar Law to be about £4,200,000,000 and the total

debt to be £3,900,000,000. This debt of approximately $20,000,000,000 is expected to increase to $30,000,000,000 by the end of the present fiscal year, and will then entail an interest charge of about $1,500,000,000 annually. The new English war taxes yield only a relatively slight amount over this interest charge.

The Policy of 'Taxation Only'

It is not to be inferred, however, that because the proposal to pay for the war by current taxation is strange in the history of war finance, it is therefore undesirable. On the contrary, it is a proposal which has many features which decidedly commend it for adoption. Our past practice certainly cannot be defended as a perfect model for the present action, and we are in such a strong position economically as compared with the other nations at war that we may well be able to withstand a more rigorous financial program than those they have used. It should be realized, however, that any taxation beyond that necessary for interest payment is unusual and is open to the uncertainties which arise when a departure is made from established practice.

It seems doubtful whether the adherents of the 'taxation only' policy realize the full practical import of their proposal. To raise the carrying charges alone on the huge sums which will be used will mean taxation of staggering weight. If we are to count on an expenditure of not far from ten billions the first year and a similar sum for a possible second year of war, it would be necessary, assuming that all current war expenses are to be defrayed by loans made on a five per cent. basis, to levy additional taxes to the extent of about $500,000,000 for the first year and perhaps one billion for the second year of war. This much at least, everyone will agree, should be covered by current taxation. The real question is how much more shall be raised at once by this method for amortization purposes and for payment of war expenses directly? Let us examine some of the arguments advanced in connection with the controversy of loans versus taxation.

Do War Loans Induce Price Inflation?

Among the arguments in support of the taxation policy is one which holds that a resort to loans would lead to an immense inflation in prices. Although some merit undoubtedly attaches to this view, its importance can easily be exaggerated. Whether public borrowing will lead to an inflation of prices depends largely on the conditions on which loans are contracted. If the subscriptions to the loan are defrayed by borrowing from the banks, such a result would undoubtedly ensue, at least to the extent that analogous subscriptions might not have been made to ordinary industrial enterprises. But if, on the contrary, there is a large loan fund in existence—if, in other words, the accumulated profits of recent years have not yet been invested, or if the subscriptions to the loan involve simply a change of investment from private enterprise to government service, there will be no such resort to credit and there will be no such inflation of prices. It is entirely probable that, as a result of our prodigious prosperity during the last year or two, a very large loan could be floated without an inordinate resort to banking credit.

Do War Loans Favor the Wealthy?

A second argument takes the form of an attack upon the loan policy. Subscriptions to loans, it is maintained, will be made by the wealthier classes who will thereby fasten upon the community as a whole an incubus in the shape of the obligation to pay them interest for a long time. This argument, however, presupposes that the tax burden, designed to defray the bond interest, will fall primarily on the poor. If, on the contrary, the general tax system is so adjusted as to recognize the principles of equality and ability to pay, the interest on the debt will be primarily defrayed by the very classes who subscribe to the bonds. If this be done, it is a matter of indifference whether the tax or the loan policy is adopted so far as the burden upon the poorer classes is concerned. The richer portion of the community will

pay the bills either way. But it is a matter of great importance to them whether they are asked to pay in two years or in ten years. The interests of the poorer classes, moreover, may be very adversely affected if the taxation policy is made so severe as seriously to cripple industry in general.

'Conscription of Wealth'

There is still another argument—one which depends for much of its force upon the attractiveness of a phrase which seems to have originated in Australia. If we are to have conscription of men, we are told we ought also to have conscription of wealth or conscription of income. But, in the first place, is it accurate to classify and to contrast in this manner? Is it proposed to draft for personal service only the poor of purse? Will not the wealthy be called upon to make sacrifices of service? The proposal to permit able-bodied men of wealth to purchase exemption from military duty by surrender of their property would certainly not appeal to anyone. When war begins to reap its harvest, there will doubtless be a full measure of distress among the wealthy. Moreover, does not this argument appear to rest to some extent upon a desire to punish and to cause suffering? Paraphrased, it would read as follows: The poor will have to suffer by rendering personal service; let us make the rich suffer also by compelling them to surrender their incomes. There will be personal service rendered by both rich and poor, and if the war continues for a long time great suffering will ensue. The sacrifices of the poorer classes certainly must not be increased by the addition of heavy economic burdens. Wherever the expenditure of money will further the purposes of the war, will prevent suffering and save life, the money must be spent. The financial burden of this must indeed be borne by those who have a surplus, and there is every indication that they will accept the burden willingly. But instead of planning our war finance in a spirit of vindictive destructiveness, every effort should on the contrary be made to render this

part of the war sacrifice as easy and convenient to bear as possible.

The Burden Should Be Distributed

Moreover, several positive considerations may be urged against the extreme form of the 'conscription of wealth' argument. For instance, the raising of all war expenses by taxation is like the pay-as-you-go policy in peace times. The objection to defraying extraordinary capital expenditures out of taxation is that it causes this year's taxpayers to contribute an undue share for benefits accruing far in the future. Meeting all war expenses by taxation makes the taxpayers in one or two years bear the burden of benefits that ought to be distributed over a decade or two.

Again, the raising of such immense sums would involve an unendurable strain upon our tax machinery. If, as will be seen later, a large part of the additional sums will have to come from income taxes, it must be remembered that the great mass of American incomes is derived from agriculture, and that of all incomes, these are the most refractory. The only result of an attempt to 'confiscate' might be the complete breakdown of the tax system.

Wealth Surplus Needed for Charity

Finally, the adoption of the 'taxation only' policy would involve a very serious diminution in the incomes which at the present time are largely drawn upon for the support of educational, charitable and philanthropic enterprises. Moreover, this source of support would be dried up precisely at the time when the need would be greatest. In calculating the advantages of the policy, therefore, it is necessary to consider the fact that the state would have necessarily to assume a number of functions now performed by private individuals, so that not only would some of the gain be more apparent than real, but there would in all probability be a considerable loss entailed by the difficult and hasty transition from private to public activities.

Considerable Tax Increases Are Feasible

For the reasons made clear in the foregoing discussion, it appears that the 'conscription of wealth' plan in its extreme form would not be feasible. It is entirely feasible, however, and it is on the whole very desirable in our present situation, to levy taxes far in excess of what has been our custom in past wars. In addition to money to pay interest on the loans, there should be raised by taxation a sum intended to secure a speedy amortization of the debt. If, as we shall see later, the debt ought to be thrown into a form which will insure its disappearance in not more than ten or twenty years, the amortization quota should amount to five or ten per cent. annually. On the assumption that a two-year war debt would amount to twenty billions, there would be needed for the amortization quota from one to two billions a year. The fiscal conclusion, therefore, would be that we should raise by new taxation for the first year of the war at least one and one-half billions of dollars (half a billion for interest, one billion amortization), and during the second year three billions (one billion interest and two billions for amortizations). When one recollects that the total federal revenue from taxation in 1915 was $625,000,000, he will appreciate what a stupendous program this implies. It involves an increase in taxation far in excess of anything that has been known in American history and considerably more than what has been attempted in Europe. To accomplish this successfully will be a magnificent triumph for our revenue system. We should indeed raise by taxation as much as we can without arousing discontent or stifling enterprise; but if we limit ourselves in this war merely to that amount without resort to loans, our participation will be insignificant and ineffective.

II. LOANS

The arguments of the advocates of 'taxation only' will probably not receive substantial support at Washington. Indeed, the first loan bill has already been presented to

Congress. In this bill, there are four chief points of interest:

1. The amount of the issue;
2. The rate of interest;
3. The term of the loan and provisions for repayment; and
4. The problem of tax exemption.

Each of these points will be briefly discussed.

1. The bill[1] provides for an issue of $7,000,000,000, of which $5,000,000,000 is in bonds. If our calculations, based on the experience of the European countries, are correct, the present issue will not suffice for our needs for the first year. It is indeed the largest loan that has ever been issued by any country and it will be a strong test of the ingenuity of our officials and the loyal readiness of our people. It is, perhaps, as large as can conveniently be handled at one time; but an additional loan is to be expected before the lapse of many months.

Rate of Interest

2. The rate of interest in the bonds is fixed in the bill at three and one-half per cent. This differs radically from the proposal made on page 30 that the loan be made on a five per cent. basis. In the first place, however, the bonds are exempt from taxation. Were the bonds to be subject to taxation, the rate of interest would have to be at least four per cent. or possibly four and one-half per cent., if the bonds were to sell at par. In the estimates made on page 30 no allowance is made for the exemption of the bonds from taxation for the obvious reason that, in the main, what is saved by the government in the lower rate of interest due to the tax-free provision will again be lost by the government through the diminished yield of the income tax. Furthermore, it must be remembered that this is only the first instalment of what is probably to become a gigantic war debt, and with every future issue on a large scale the rate of interest will

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[1] A copy of the War Finance Act as finally passed will be found on page 129.

doubtless increase. There is not much reason to expect that in a short time our credit will stand very much higher than that of the other warring countries, or that investments in government paper will be possible at a much lower rate of interest than in secure investments of a private character. The destruction of capital, which is going on at such an enormous rate, will tend to bring about a gradual rise in interest rates. It therefore still remains a conservative estimate that the loans of the United States will be issued on an average of a five per cent. basis.

Ten or Twenty Year Bonds Preferable

3. The terms on which the loan is to be issued are not fixed in the bill, but are left entirely to the discretion of the authorities. This is true, even of the length of the loan. It is obvious that the longer the loan, the more favorable the conditions under which it can be marketed; but it is true also that long term bonds, say for thirty or fifty years, are of questionable advisability in other respects. In the case of countries which have no objection to perpetual debt, such bonds may be defensible; but there have always been and are today valid objections to perpetual debts in the United States. Since every generation may be expected to have troubles of its own, it is clearly a part of wisdom for any nation, which can possibly afford to do so, to pay off its debt within the generation which contracted it. Our experiences, moreover, with the bonds which were issued during the great refunding operations after the Civil War, even though their length was only thirty years, were sufficiently disheartening. Although there was a large balance in the Treasury during the '80's, we were unable to pay off the debt except through the very costly medium of buying long term four per cent. bonds in the market, often at a premium of from twenty-eight to thirty per cent. The government should profit from this experience, and should issue bonds to run for not more than ten years or, at the outside, twenty years.

PUTTING UP THE FIRST WAR BOND SIGN
National Bank of Commerce Building, Nassau and Cedar Streets, New York City

Provisions for Repayment

Still more important, however, is the arrangement for repayment. Most of the loans issued in this country have been so-called 'straight' bonds, all of which mature at the same time, with a more or less adequate sinking fund system. The sinking fund provisions in our loans of the Civil War have, as is well known, never been considered of a binding character. They have been rather bookkeeping devices, and the government has paid off from year to year either more or less than the nominal sinking fund requirement, according as the exigencies of the time demanded. In our state finance, the abuses of sinking funds have been very notorious of recent years and have led, in not a few states, to the introduction of the so-called serial bond system whereby a certain proportion of the issue is retired annually. Almost no attention has been given in this country, however, to other forms of bond issues which provide for retirement in either regular or irregular instalments. A study of the history of public credit will show that there is a great variety of issues possible, and that many of the methods practised, especially in the local finance of some of the European countries, are well worth consideration by our government. However that may be, one conclusion is certain, namely, that from the very time of issue adequate provision should be made for an annual amortization quota so arranged that at the expiration of the life of the loan, the entire debt will be virtually extinguished. It would be deplorable in the extreme if such gigantic issues as we have in contemplation were to be made with the simple prospect of refunding the loans at some future time, particularly, in view of the strength of our present economic position. A perpetual debt or even a long debt must be avoided.

Tax Exemption Problem

4. Finally, the question of the exemption from taxation must be considered. The argument in favor of exempting loans from taxation is that they will sell at a

higher price and thus net the government more than they otherwise would. While this argument is of some weight in times when the credit of the government is seriously impaired, at a time like the present it has but little force. Moreover, the argument on the other side is far stronger. If, as seems entirely likely, a large part of the necessary revenue will have to be raised by a greatly enhanced income tax, it is the height of injustice to divide the population into two classes and to exempt from burdens the holders of government bonds. From the point of view of equality of taxation, there is no warrant for this. On the contrary, the investors in government bonds, like investors in all other forms of capital, enjoy what is called in the English tax an unearned income, and virtually everywhere in Europe an unearned income is taxed at a higher rate than an earned income. In this country, however, we should be adopting a double injustice: we should not be taxing the owners of bonds at a higher rate than the recipients of earned incomes, but we should as a matter of fact be taxing them at a lower rate.

Another argument often advanced is that it makes practically no difference whether or not bonds are tax-free. For if the purchaser of a government bond knows that he is to be exempt from taxation, this exemption will be capitalized into a difference in the selling price, and he will pay so much more for the bond or—what is equivalent to the same thing—will receive so much less interest. This assumes, however, that it is known in advance what the rate of the income tax is going to be. But in the present situation that is manifestly impossible. The subscribers for our proposed government bonds will, at a given rate of interest, pay a price which is calculated on the exemption from the present income tax, and from an estimated future income tax. But what the increase in the income tax will be in the near future no one can tell, and it is obvious that this unknown increase of the tax cannot be accurately capitalized. Therefore, to the extent at least of any future unexpected increase in the income tax, the holders of bonds will enjoy an unmerited exemption. They will not be sharing the burdens with the rest of the

citizens. Instead of paying a higher tax on the unearned income, they will be paying a lower tax.

Another Tax Exemption Injustice

Moreover, to exempt the bonds from taxation will cause injustice in yet another fashion. Our income tax is now highly progressive, and in the new income tax the progression may be made even more pronounced. The bonds, if issued as proposed in the present bill, are exempt in the hands of the holder whether he be a man with an income of five thousand or five million dollars. It can easily be seen that the exemption provision will have the practical effect of nullifying to a considerable extent the progressive rate of the income tax. The newspapers report that the new issue will be a 'rich man's loan' because of the eagerness of the payers of the super-tax to insure themselves against the probable increases in taxation. If the entire issue were taken by the taxpayers who fall in the highest super-tax group, if there were among them entire freedom of competition in subscribing for the loan, and if there were definite knowledge of what the future would bring in the way of increased income tax rates—then, and then only, would the exemption of the bonds from taxation have any basis in justice. These conditions, of course, cannot be met.

Lessons of Recent English Loan

The lessons of the recent English loan are very significant. We are told that, of the entire issue of about £1,000,000,000, only an insignificant fraction was subscribed for in the four per cent. tax-free bonds and that almost the entire sum was subscribed for in the five per cent. bonds, not free from taxation. This shows that the English investors prefer to take their chance of a future reduction of the income tax from the present high level. But it shows above all that England is on the right track in putting its loan virtually in the shape of bonds that are not exempt from taxation. The bondholder takes his chances equally with the rest of the community.

The American practice of issuing tax-free government bonds dates from a time when equality of taxation was not considered the controlling consideration. In the half century since the Civil War, great progress has been made in the realization of this conception, and almost uniformly abroad the tax-free provision has been eliminated from government issues. It is high time that this should be done also in this country. The present bill, unfortunately, makes only a slight concession to this demand. It makes the new government bonds liable to the estate tax. But the logic of this exception would impel to the total abandonment of the entire tax-free clause. In its present form the provision is both illogical and unjust.

III. TAXATION

According to our calculations, $1,500,000,000 of additional revenue will have to be raised this year, and some $3,000,000,000 the following year if we are to do our full share in the war, and at the same time to avoid shifting the burden too far into the future.

The reasons for heavy levies of taxes are clear. In the first place, it is always easier to impose severe burdens upon a community at a time when feelings of loyalty are aroused. Sacrifices are then made willingly which in ordinary times would cause much complaint. The capitalization of patriotism in this fashion for the accomplishment of national tasks is the height of financial wisdom.

The actual burden of taxes, moreover, in time of war is less than it appears to be. Not only are immense profits secured by the war contracts apt to be more or less diffused throughout the community in the shape of high wages and a greater demand for materials, but, in addition, the higher level of prices which usually accompanies war makes a given tax a much smaller actual proportion of consuming power than under ordinary circumstances.

Finally, from the general economic point of view, it is far better to levy high taxes during a war, when the social income is great, and the diversion of income to ordinary investment of capital relatively small, than

to postpone the taxes necessary to sink the debt until after the war, when the need of capital investment will again become acute.

Taxation and Sound Economics

From every point of view, therefore, as much money ought to be raised during the war by taxation as is consistent with a sound economic progress. According to our analyses, it is desirable to raise as much as $1,500,000,000 this year and $3,000,000,000 the following year. But how is such a gigantic sum of money to be secured? What are the possible sources of revenue?

In former wars, both in Europe and in America, where the accumulation of wealth was comparatively small, and where the ideas of equality of taxation had not yet permeated the popular mind, it was possible to elaborate a system of taxation which, to a great extent, perpetuated the traditional system. This traditional system burdened primarily the consumption of the community and exempted its productive wealth. With the progress of democratic conceptions in taxation, all this has been changed. Of late, more and more stress has come to be laid on the idea of income and property and less on the criterion of expenditure. If we look at the practical possibilities of our American system, in the light of recent European experience, we shall see that there are only five possible sources of war taxation, each of which will be considered in turn.

1. The Property Tax

The attempt to raise any large sum by the taxation of property as such may be eliminated from consideration. For familiar reasons, which need not be recounted here, the general property tax has everywhere broken down in our state and local finance. It has become, in large part, a taxation of real estate, whereas what is needed at the present time is primarily a taxation of personal property and especially of intangible wealth. We have no taxing machinery in the federal government

and it would probably be impossible to devise any machinery which would make a property tax an administrative success. The only one of the warring countries which has made the attempt to levy a large property tax is Germany where, for special reasons, a workable scheme of assessing property values has been elaborated in the course of the last few decades. Even in England this has not been attempted. In the United States this whole plan may, for the immediate future at least, be dismissed as impracticable.

2. The Inheritance Tax

The present estate tax as modified by the legislation of a few weeks ago, is calculated to produce $100,000,000. It is a tax at progressive rates, graded from one to fifteen per cent. The English system of death duties, with rates considerably higher and with a far lower limit of exemption, produces about $150,000,000 a year. There is no doubt that we could also secure a considerable augmentation of the yield by lowering the present exemption of $50,000. But in contemplating a great increase in the progressive scale of the estate tax, it would be necessary to remember that there are also state taxes on inheritances, the rates of which in some cases run up to fifteen per cent. At present, therefore, in parts of this country, we already have a system of inheritance taxes up to thirty per cent., a scale which is appreciably higher than anything existing in the great European countries. Any attempt considerably to increase the rates of the inheritance tax would have to be attended by at least two modifications. In the first place, there would have to be some sort of accommodation between state and federal taxation of inheritances, with a provision that those states which derive a large revenue from this source should be compensated in some way. In the second place, if the rates were to be made very much higher than at present, it would be necessary to introduce the system now in vogue in some other countries, guaranteeing against a repeated payment of the tax on the same estate within

a few years, if by chance the existing successive owners should die within a short period of each other.

Taking all these facts into consideration, it is not likely that any practicable change in the inheritance tax, even though it involved both an increase of the graduated scale and a decrease of the exemption, would net more than one hundred millions of additional revenue.

3. The Income Tax

The federal income tax this coming year is expected to yield about $250,000,000, approximately the same amount that Great Britain raised through her income tax before the war. The income tax in Great Britain is expected to yield this year about $1,000,000,000, that is, about $750,000,000 more than before the war. The question then arises: Can we not do the same? In what way can we also, possibly, quadruple the revenue from our income tax? This is an interesting but a difficult field of inquiry.

It is undoubtedly true that our social income is very much larger than that of England. Before the war, the English wealth was roughly estimated at about $80,000,000,000, the German wealth at about $85,000,000,000, and our wealth at about $200,000,000,000 (the official figures for 1912 were $187,000,000,000). All such estimates are indeed of the vaguest possible character. But taking them for what they are worth, it would follow that the income of the United States would be about two and one-half times that of Great Britain, making no allowance for a possible higher percentage of expected as compared with realized income in the United States. If, therefore, we had the same rates of the income tax as in England, it might be claimed that our revenue ought to be two and one-half times as great. Two important facts, however, must be remembered. In the first place, the exemption from the income tax in England is £130 or $650, whereas our exemption from the income tax is virtually $4,000. Far more significant than this, however, is the fact that in an industrial country like England the great

mass of the total incomes is derived from industry and trade, and that even the incomes from land are paid in great part by the large landowners. In the United States, however, the great mass of incomes arise from agriculture and are small in amount. Of all incomes, small farmers' incomes are proverbially the most refractory. In the statistics of the Wisconsin income tax published by the state tax commission, it appears that in 1916 the farmer paid only 3.86% of the state income tax, as over against 20.30% paid by manufacturers and 27.23% paid by merchants and bankers. If Wisconsin may be taken as a fairly typical state, it is obvious that an immense deduction from the taxable income must be made for the agricultural incomes of the United States. It would not be at all safe to argue from British to American conditions.

Effect of Tax Exemption Reduction

It is important, however, to raise the question as to how much additional income tax could be secured by a considerable reduction of the exemption. Here again a surprise awaits us. Of the total income tax in the year 1914–1915, amounting to some $124,000,000, the proportions raised were, in round numbers, as follows:

Corporation tax	$56,994,000
Individual tax:	
Normal tax	23,996,000
Additional tax	43,684,000

In other words, the additional tax was almost twice as large as the normal tax.

The additional tax was subdivided according to the following categories:

Incomes from	$20,000 to $100,000	$13,706,000
Incomes from	100,000 to 500,000	17,330,000
Incomes over	500,000	12,648,000

Wisconsin Income Tax

The Wisconsin tax statistics show that the taxpayers with incomes up to $4,000 paid a tax of $517,520 out

of a total tax on all individuals of $1,601,213. That is to say, with an income tax exemption of only $800,[1] about one-third of the tax was paid by recipients of incomes under $4,000. It is manifestly out of the question, however, to assume that the federal exemption will be reduced to as low as $800. If we take $1,500 as the lowest probable figure of exemption from the federal income tax, we find that, to judge from the Wisconsin figures, we should be adding only about sixteen per cent. or one-sixth to the receipts from the income tax. In England, on the other hand, the proportion of taxes paid by the relatively lower incomes in certain schedules is considerably greater. In 1914, these were the figures for the taxable income of certain taxpayers in schedules D and E, that is, the ordinary commercial and industrial incomes.

Income	*Gross Taxable Income*
Below £300	£49,112,279
£300 to £600	25,421,620
£600 to £800	6,309,844
Total	£80,843,743
All incomes	£115,363,615

British Income Tax

In other words, in these particular schedules, over two-thirds of the taxable income was found in the case of individuals with an income under £800 or $4,000. £800 in England, however, probably means relatively more than $4,000 in the United States. The above figures apply, moreover, only to partial incomes in a particular category. It is entirely probable, therefore, that the additional revenue to be expected by a reduction of the exemption would be very much closer to the one-sixth, as represented by the Wisconsin figures, than to the two-thirds, represented by the English figures. Thus, for every one per cent. of income tax, which, as we have seen, meant about $24,000,000 last year, it would not be safe to add more than a third for the additional revenue to be

[1] $1,200 for man and wife.

secured by the reduction of the exemption to $1,500. In other words, for every one per cent. of income tax, the normal tax would represent about $32,000,000, instead of $24,000,000.

How Heavily Shall We Tax Large Incomes?

The English income tax is now levied at a rate of from about twelve per cent. to a rate amounting to about thirty-four per cent. on the highest incomes. If our normal rate were to be ten per cent., instead of the existing rate of two per cent., the revenue from the normal tax on individuals would be about $240,000,000, if we kept the present exemption (ten times the yield of last year at one per cent.), or some $320,000,000 with a reduction of the exemption to $1,500. As against the fifty millions awaited this year from the two-per cent. normal tax, this would mean an additional revenue of some $250,000,000. However, if the same rate of ten per cent. were applied to the corporation tax, we should get another $500,000,000. The additional tax still remains as a resource. With the rates running up to six per cent. last year, it yielded $43,000,000; yet the total estimated revenue of the income tax for the present year, with a normal tax double the year before, and with an additional tax running up to thirteen per cent., is expected to be only about twice as great. In order, therefore, to secure any very large revenue from the additional tax, the rates would have to be increased considerably above the present figures. In order to secure $200,000,000 or $300,000,000 from the additional tax, the rates of the additional tax would have to run up to thirty-five or forty per cent., which, added to the normal tax of ten per cent., would mean a rate of some fifty per cent. on the highest incomes.

It follows, therefore, that if we try to secure an additional revenue of $1,000,000,000 from the income tax, it would be necessary to reduce the exemption to $1,500, to make the normal rate about ten per cent. and to graduate the additional rate up to forty per cent. (or a total of fifty per cent.). This is very much higher than what exists

in England at the present time, and probably fully as high as could be well endured. Moreover, with such rates, it would be imperative to make a distinction, as the European countries do, between earned and unearned incomes, taxing the unearned incomes at a lower rate. This would considerably reduce the revenue from the tax. Finally, another notable diminution of the yield would follow the unfortunate exemption of interest on the new and gigantic war debt. With every billion dollars of new tax-free debt there would be a reduction of from ten to twenty millions in the yield of the income tax.

General Conclusion on Income Tax

The general conclusion, therefore, is that it would be practicable to secure an additional revenue of perhaps $750,000,000 from the income tax by a system which would grade the tax from about ten per cent. on moderate incomes up to forty per cent. on the highest incomes, and with a proportionate reduction of the rate on lower incomes down to $1,500. But the adoption of such an extremely high income tax would call for the greatest care in recasting certain features of the law which even now, with a low rate, are producing inequality and discontent.

4. Excess-Profits Tax

Since the inheritance tax will yield comparatively little, and since the income tax can be counted on for only $750,000,000 of additional revenue, recourse must be had to a method that has been employed in Canada, Australia and almost everywhere in Europe and which is already being used to a certain extent in the United States, *viz.*, the taxation of excess profits. Last September, Congress passed an act placing a levy of twelve and one-half per cent. on the net profits of munition manufacturers.[1] Only a few weeks ago, there was added to this a small tax on excess profits in general.

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[1] In the case of the munition manufacturers' tax, the levy is made against all net profits without the eight per cent. allowance.

Much might be said, in this connection, concerning the desirability of government action in the direction of price control, particularly the control of the prices of war materials. The enormous purchases soon to be made will be a disturbing element in the market situation—one which will destroy many of the ordinary safeguards of free competition. Price regulation, which would effectively restrict prices to a point near the cost of production, would be preferable to high prices, high profits and a high excess-profits tax. Price regulation would mean a diminution, of course, in the fiscal results of the excess-profits tax.

Our Excess-Profits Tax upon an Arbitrary Basis

There is a great and important difference between the European taxes and our own excess-profits tax. All of the European laws measure taxable profits by comparing present profits with the average profits of business before the war began; in some cases this average is taken for a number of years. Our law, however, takes the arbitrary figure of eight per cent. on the "capital invested" (plus $5,000)[1] as the normal profit and taxes everything above that eight per cent.

This arbitrary method is unfair both to investors and to industry. Especially in a comparatively new country like the United States, where risks are great and losses frequent, a profit of more than eight per cent. is often necessary to justify investment. At the present rate, the situation is not serious; but with the necessity of levying a far higher rate, the continuance of our present method would involve us in difficulties. At a period like the present, it is of the first importance not to put a check upon business enterprise or to cripple the desire of individuals to do their utmost in the way of productive capacity. The principle of taxing very heavily excess profits above normal peace profits is indeed defensible; but to penalize all profits above eight per cent. applied to

1 "Capital invested" is defined to include cash paid in, the cash value at the time of payment of capital represented by property and surplus invested in the business.

a base such as that prescribed in our present law can scarcely be defended. Instead of bringing any more revenue, a larger rate upon such excess profits might yield actually less revenue, in addition to placing an unfair burden upon a particular class of investors. It cannot be emphasized too strongly, therefore, that if we are to have a high excess-profits tax, we should follow the European principle and abandon the arbitrary methods now being followed.

Probable Returns from Excess-Profits Tax

The yield of the present law is problematical, but it has been roughly calculated that the returns will be between $200,000,000 and $225,000,000. A very vague estimate, made some time ago, figured that the excess profits last year were about $5,500,000,000, but that the deductions and exemptions in the law reduce the taxable excess profits to some $3,000,000. In Great Britain, the excess-profits tax was estimated to yield in the fiscal year just ended between $400,000,000 and $500,000,000. But it will probably yield between $600,000,000 and $700,000,000. The English tax is levied at the rate of sixty per cent. While our excess profits have been exceedingly great, it is doubtful whether they have been much larger than in England where the profits have come not only from the war expenditures, but also from the immensely enhanced returns from shipping. In order to secure $500,000,000 more from the excess-profits tax in this country, it would be necessary, assuming that the suggested change be made in the base line from which to measure the excess of profits, to increase the rate to forty or fifty per cent. It might be advisable to take as a basis, not only the profits of the current year, but the average of the excess profits of the last two or three years, in which case the yield would be largely increased.

5. Indirect Taxes

If the rates of the income tax and of the excess-profits tax were raised to the height suggested during the first

year, sufficient revenue might be obtained for the needs of that year without other taxes. It is possible, of course, that much more might be obtained than has been estimated. At any rate, valuable experience would be gathered and a more definite basis for future calculations would be made available. If the machinery of direct taxation appeared to be in no danger of breaking down, it might be possible even to make further increases in rates. If, on the contrary, the yield of the first year's taxes was disappointing, or if it seemed wise not to raise the rates to the suggested maximum at once, there would still remain the whole field of indirect taxation.

Increase in Taxes Abroad

It is perhaps significant that all of the warring countries have found direct taxation alone to be insufficient. In Germany, where immense additions have been made by the localities and the separate states to the income taxes, the federal government has imposed large burdens, not only on excess profits, but also through indirect taxes. The same is true to a still greater extent in France. In England also, the revenue from indirect taxes, and especially from customs and excise, has been very largely increased as appears from the following figures:

Tax	1914	1916
Customs	£35,569,000	£57,707,000
Excise	39,658,000	61,210,000

The figures for 1917 are not yet available, but they are expected to show a further increase. In other words, England has secured an additional revenue of about $250,000,000 from the customs and excise duties alone, having imposed higher taxes on tea, sugar, coffee, railway tickets, and a variety of other items. In the United States, our revenue from the tariff is about $100,000,000 less than the British revenue from her free-trade tariff.

Our Civil War Experience

Our Civil War experience indicates the rich productivity of indirect taxation. If we were to tax certain

articles at the rates customary in the Civil War, it would be easy to secure an immensely enhanced revenue. From calculations which were printed in a detailed table appended to the recent report of the Committee on the Relations of State and Federal Taxes, submitted in January to the Seventh Annual New York State Conference on Taxation, it appears that the revenue from certain taxes on commodities, if levied at Civil War rates, would, during the coming year, be about as follows:

Source	*Estimated Revenue in* 1917
Tobacco	$305,000,000
Distilled spirits	272,000,000
Petroleum	282,000,000
Cotton	120,000,000
Iron and steel manufactures	122,000,000
Cotton goods	53,000,000
Woolen goods	36,000,000
Boots and shoes	44,000,000
Coal	31,000,000
Railroad passenger tickets	82,000,000
Leather	26,000,000

Moreover, it may be recalled that in 1916 some $42,000,000 was raised in the United States by stamp taxes. This source yielded England about $35,000,000 last year. Probably as much as $75,000,000 could be collected by such a tax without making the rates exorbitantly high.

This list could be extended almost indefinitely.

While it is obvious that it would be unwise to levy all or even a large proportion of these taxes, it is clear that certain commodities might be chosen and that the tax might be so graduated as to fall primarily on the better qualities of the goods rather than on the necessities.

In any event, it would be comparatively easy to raise a few hundred million dollars from such indirect sources. This system, as a supplement to the vastly more important direct taxes, would probably suffice for the first year or two of the war. Were the war to continue for a longer period, it would be necessary, of course, to revise all our calculations.

Conclusion

In conclusion, it may be pointed out that since this war is being prosecuted on a gigantic scale, our expenditures and our revenues must be expected to be on the same scale. All preceding ideas on the subject must be thrown in the scrap heap, together with the similar views as to the military conduct of the war. Of one thing, however, we may be assured. The prodigious wealth and the unexampled prosperity of the United States ought to leave no doubt as to our ability, not only to finance the war, but to finance it successfully and equitably. **But in the utilization of our enormous resources, it becomes all the more important to develop a system which will conform to sound economic principles and which will be in harmony with modern ideas of equality and justice.**

THE LARGEST WARRANT EVER SIGNED

Secretary McAdoo signing the warrant which gave $200,000,000 to the British government. The first step by the United States to help her allies.

Left to right: LORD CUNLIFFE, Governor of the Bank of England; SIR CECIL SPRING-RICE, British Ambassador; WILLIAM G. MCADOO, Secretary of the Treasury; SIR HARDMAN LEVER; SIR RICHARD CRAWFORD; OSCAR T. CROSBY, Assistant Secretary of the Treasury.

PART III.

Financial Management of a War

Financial Management of a War*

By HENRY C. ADAMS, Ph. D., LL. D. †

The prosecution of a war of such magnitude as to call for large expenditure of money, imposes upon the minister of finance the duty of adopting a policy for the management of the public treasury. Under modern industrial conditions, however, his choice is quite restricted, for there are but three proposals which it is worth his while to consider. These proposals are as follows:

1. The entire war expenditure may be drawn from newly-levied taxes. In the administration of this policy the only loans required are loans in anticipation of tax receipts, in order to cover the demands upon the treasury during the period in which the new revenue system is becoming operative.

2. The entire expenditure of the war may be met from the proceeds of loans. In this case there is a call for new taxes equal to the interest upon the loans contracted. Sometimes even interest payments are met by selling new bonds, but this is so manifestly at variance with sound rules of finance that it need not be considered.

3. The extraordinary expenditure entailed by the war may come from a reasonable union of these two sources of revenue—loans and taxes. The important question presented by this policy pertains, of course, to the nature of the union proposed, and to the ratio of proceeds by loans to proceeds from taxes; and it is further necessary to inquire if this ratio is the same for all stages of the war.

It must be remembered throughout the investigation, in this manner laid before us, that our problem has primarily to do with extraordinary expenditure—that is to say, with expenditure over and above the demands of peace.

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Nor does this properly present the extent of the treasury problem. It is more than likely that some of the ordinary sources of revenue will be cut off by a state of war, so that new ways of securing money must be opened to cover the deficits in permanent demands. An adequate financial policy, therefore, must be more than sufficient to make headway against war expenditures.

Shall the entire extraordinary expenditure entailed by a war be met by an exercise of the taxing power?

This question brings us at once into the presence of a claim respecting which there is great diversity of opinion. There are those who assume, without proof or argument, that a people engaged in an exhaustive conflict are unable to bear any marked increase in taxation so long as the conflict shall continue. There are others who, stopping short of this extreme claim, yet urge it as highly desirable that the burden of a war should be distributed over several generations. From such premises the adoption of the loan policy must logically follow. As opposed to such opinions, there are writers of respectability and standing in finance who deny the inability of a people to meet within the year all necessary expenditures, and who refuse assent to the time-honored argument that by a loan the burden of a war may be distributed. Such writers claim that the generation engaged in the contest must bear the burden of its expense; that this burden can in no manner be bequeathed; but that, if the war entail a debt upon the following generations, its burden is borne twice—once by the fathers who furnished the capital that was destroyed, and once by the sons who furnished the money to expunge the debt. Although this latter conception of war expenditure does not appear to me to be quite accurate, it is yet based upon the manifest truth that each generation must subsist upon the product of its own industry. No father can eat the potatoes to be hoed by an unborn son, nor can an army live on bread to be delivered, at the option of the baker, between ten and forty years from the date of the contract. It is thus the production of the past and the present, and

not that of the present and the future, which furnishes the required capital for a war.

Such a statement of truisms, however, is no final argument in favor of the taxing policy, nor does it meet fairly the claim of those who say that by means of loans the burden of a conflict may in part be thrown upon posterity. They who claim that war expenditure should be entirely met from the proceeds of taxes fail to recognize two very important facts. In the first place, they fail to understand the difference between capital expended in a war and the burden entailed upon the citizens of a country by a war. The consumption of capital may or may not give rise to the consciousness of extraordinary expenditure on the part of the state, according as it does or does not effect involuntary privation. The real burden of a war consists in the fact that men are deprived of property without the compensation of hope. In the second place—and here lies the kernel of the argument—they fail to perceive that the most important factor for the financier is not the material but the psychological factor. It stands as a first principle in an adequate war policy that, however great may be the demand for a current year, it should be met in such a manner that the source from which supply is drawn may never be exhausted. The appeal of the financier to the industrial producers should be made in such alluring language that, while continually giving of their product to the state, their energy will never be slackened. The fund of current product, from which all revenue is drawn, should be as unfailing as the widow's cruse of oil.

It may appear at first glance that the realization of this principle in actual treasury management is impossible; but it is perfectly feasible, provided only a proper financial policy be adopted. It is an error to suppose that current consumption in time of war is largely increased over average consumption in time of peace. Public consumption may be greater, but private expenditure is curtailed. Unless mercenaries are brought from abroad, no more of the necessaries of life are required than before the mobilization of the army, and on the average such as are consumed will be of no better quality. To balance the

increase of capital required for the manufacture of arms, powder, ships, and the like, there is a decrease in the rapidity with which capital is invested in forms adapted to peace employments. It is, however, necessary to notice that average production can only be maintained by unusual exertion on the part of non-belligerents, for the ranks of peace workers will have been depleted by enlistments in the army. This call for increased activity is, in reality, the first tax sustained by those who continue to follow the common pursuits of life. But this tax need not be the occasion of solicitude, for common habit may be relied upon to tide over this first draft of men from the industrial ranks. A farmer who, with three sons, has been accustomed to cultivate a section of land, will not permit a hundred and sixty acres to lie fallow because one of his sons has joined the army. It is a truth of quite general application that men are disinclined to fall below a standard once achieved; and it is upon the principle of human nature which this truth discloses that the financier may rely for the maintenance of average production, notwithstanding the reduction in laboring force.

The real question that confronts the financier is the following: Can he expect this increased activity will be maintained if, in addition to the labor-tax, he levy a money-tax equal to the entire expense of supporting the army? To answer this question in the negative is not to deny whatever is true in the claim that taxes tend to quicken production. A tax levied for that purpose must gradually and persistently, and through a long series of years, raise the rate which it imposes; the desired result would not follow should industries be subjected without warning to excessive charges. For example, is it reasonable to believe that the industry of the Northern States would have been rendered more intense if the total expenditure of 1862 had been met by taxation? The expenditure of that year was equal to one quarter of the total national product, while the extraordinary war expenditure was equal to one fifth of such product. Assuming that newly levied taxes might have secured the money for 1862, can one suppose that the year 1865, when war

expenditure amounted to twenty-seven per cent of gross product, would have furnished an adequate amount of disposable capital? No one who understands the psychology of taxation can for a moment admit such a claim. A tax so excessive in amount, precipitated without warning upon established industries, would have encroached upon working profit, weakened the incentive to labor, broken the mainspring of activity, and destroyed the mechanism of production. It would, therefore, have disregarded the first principle of treasury management, for it would have dried up the source from which all revenue must come. An adequate policy for the conduct of a war must be able to carry a people through to the end, and not expose them to the danger of a stranded treasury in the midst of conflict.

If, on the other hand, a part of the extraordinary expenditure should be met by an appeal to credit, the loans would be largely absorbed by free capital. This would cause no derangement of existing industries, and the saving in this manner secured would be voluntary saving. The idea of loss would not attend the payment of capital to the state, but rather the thought of establishing a permanent income would induce to renewed activity. The administration, therefore, would run no risk of exhausting the fund from which future revenue might be secured, for it would be continuously replenished by willing hands. It is altogether by the mark to say that loans must in the end be paid from the proceeds of taxes, and that, in consequence, the advantage of an appeal to credit is apparent rather than real. The question is, whether the desire to avoid taxes in the future will induce men to suffer the burden of present payments. If they truthfully declare such willingness, there can be no necessity of resorting to credit. But if, as an analysis of character declares, the potency of motives is inversely as the remoteness of interests concerned, this abstract truth, that taxes must finally equal the sums borrowed, can not be relied upon to induce men to practice self-restraint in consumption, or to undergo severe toil in production. It is such considerations as

these that lead us to regard the taxing policy as inadequate to the demand of an exhaustive war.

Shall the extraordinary expenditure imposed by a war be covered entirely by the proceeds of loans?

The policy which is here brought to view has been a favorite one with many financiers. The general claim in its favor is that, while a people are engaged in war, their industries should be freed from all unnecessary incumbrances, in order that they may supply the "extra product" which the "extra consumption of the government" demands. The conclusion of such reasoning is that, while a war lasts, no new taxes should be imposed.

It has been already observed, in the foregoing discussion, that the conception here presented is erroneous. The consumption of a people engaged in war is not greatly in excess of peace consumption. It may, if necessary, be brought down to less than peace consumption. An adequate financial policy demands only that average production should be maintained. It is true that average production calls for more intense application on the part of non-belligerents, but, if business men are not discouraged by an erroneous financial policy, the industrial habits of the people may be relied upon to attain this end. Indeed, the administration may reasonably hope that a certain amount of taxes will be willingly paid, in addition to what was termed above the labor-tax. The motive or force which the financier must call into play to secure so desirable an end is patriotism. If the purpose of the government be fully appreciated and approved, a free people will gladly undergo extensive sacrifices in order to carry out an adopted policy. It is a recognized fact that self-governing peoples are stronger for tax purposes than the subjects of a monarchical state, for their will lies more closely to the heart of the state. But the administration of a self-governing people should never undertake a war in favor of which there is no strong sentiment. As things go, then, in democratic countries, it does not appear that loans to the full extent of extraordinary demands are

necessary, and there is no question as to the superiority of taxes over loans when their use will not curtail industrial energy. The measure of this first money-tax should be the popular enthusiasm for the war.

What, however, is the specific argument against the policy of securing the entire war revenue from loans? Many considerations might be presented showing the dangers that beset this method of financiering, but a study of certain attempted realizations of it may, perhaps, disclose its inadequacy the most clearly. There are very few cases in which a struggle of any magnitude, testing at all a people's financial resources, has been carried to a successful issue on the basis of a loan policy; while there are many instances of an abandonment of this policy during the progress of a war, which itself must be accepted as confession of a failure. Twice in the history of our country has this fatal overconfidence in the sufficiency of public credit brought a rich and energetic people to feel the stress of money demands, and to experience the evils of ruinous and expensive methods of treasury control. It is not true that the actual failure of any policy proves the impossibility of its success; but it is true that a careful study of several failures will permit one to decide whether continued ill-success is due to inadequate management or to erroneous principles in the policy itself. Understanding, then, the limitations rightfully placed upon all arguments from history, let us turn our attention to the financial conduct of the two great wars in which the United States has been engaged—that of 1812 and that of 1861.

The financial policy which was adopted for the conduct of the war of 1812 finds its first statement in the treasury report of 1807. This has been called the war-report of Albert Gallatin. The reason why so astute a politician forced this question thus early upon the attention of Congress may not, perhaps, with clearness be determined; it is sufficient for our present purpose to notice the fact. The financial condition of the treasury at this time was as follows: The permanent revenue of the country was estimated at $14,500,000, while the permanent expenditure for peace purposes was estimated at $11,600,000.

In this expenditure, however, there was included an annual payment on account of the debt-service of $8,000,000, which would be reduced to $3,400,000 after 1808, because of the inability of the government to proceed as rapidly as heretofore in the expungement of the debt. Taking this into the account, the permanent expenditures on a peace basis could not exceed $7,000,000, and this would provide a permanent annual surplus of $7,500,000.

It was in the presence of such financial prospects that the Secretary spoke his views on the proper method of treasury administration in the event of a commercial war. His plan may be the best presented in his own words, which are as follows:

> That the revenue of the United States will, in subsequent years, be considerably impaired by a war, neither can or ought to be concealed. It is, on the contrary, necessary, in order to prepare for the crisis, to take an early view of the subject, and to examine the resources which should be selected for supplying the deficiency and defraying the extraordinary expenses.
>
> There are no data from which the extent of the defalcation can at this moment be calculated, or even estimated. It will be sufficient to state—1. That it appears necessary to provide a revenue at least equal to the annual expenses on a peace establishment, the interest of the existing debt, and the interest on the loans which may be raised. 2. That those expenses, together with the interest of the debt, will, after the year 1808, amount to a sum less than $7,000,000; and, therefore, if the present revenue of $14,500,000 shall not be diminished more than one half by a war, it will still be adequate to that object, leaving only the interest of war-loans to be provided for.
>
> Whether taxes should be raised to a greater amount, or loans be altogether relied on for defraying the expenses of the war, is the next subject of consideration.
>
> Taxes are paid by the great mass of the citizens, and immediately affect almost every individual in the community. Loans are supplied by capitals previously supplied by a few individuals. In a country where the resources of the individuals are not generally and materially affected by the war, it is practicable and wise to raise by taxes the greater part, at least, of the annual supplies. The credit of a nation may also, from various circumstances, be at times so far impaired as to leave no resource but taxation. In both respects the situation of the United States is totally dissimilar.

There is no question but that the Secretary here expresses full confidence in the adequacy of the loan policy to

meet the financial stress of a war. It is true that he suggests the levy of certain new taxes, but their purpose is "to provide for the interest of war-loans, and to cover deficiencies in case the existing revenue should fall below seven millions of dollars." He does not contemplate taxation as a means of defraying war expenditure.

A clearer statement of this policy is to be found in the report of 1808:

> No internal taxes [says the Secretary], either direct or indirect, are therefore contemplated, even in the case of hostilities carried against the two great belligerent powers.

And the report of 1809 comes back again to the same thought:

> Loans reimbursable by installments, at fixed periods, after the return of peace, must constitute the principal resources for defraying the extraordinary expenses of the war.

So far, then, there can be no question as to Mr. Gallatin's views respecting the financial conduct of a war; but the impression has somehow arisen that the events of the years 1810 and 1811 caused him to modify the opinions which he had previously expressed, and to urge upon Congress the adoption of taxes to a degree wholly at variance with his original plan.[1] There is, however, no evidence which warrants one in the belief that the Secretary had abandoned the theory of loan financiering; but, on the other hand, in a letter of January 10, 1812, addressed to the chairman of the Committee of Ways and Means, there may be found a restatement of the loan policy, perfect in every essential particular. It is true that the committee was recommended to urge the establishment of both direct and indirect taxes, but this was due to the fact that customs revenue had fallen below the estimates of peace demands. These taxes, therefore, could not with propriety be termed "war-taxes," since their proceeds were to be devoted to cover peace expenditure.

> It may be proper to repeat [wrote Mr. Gallatin] that so long as the public credit is preserved and a sufficient revenue is provided, no doubts are entertained of the possibility of procuring, on loan,

[1] Cf. Adams's "Life of Gallatin," pp. 450-455.

the sums wanted to defray the extraordinary expenses of a war, and that the apprehensions expressed relate solely to the terms of the loans, to the rate of interest at which they can be obtained.[1]

Again, in another place, he says: "In proportion as the ability to borrow is diminished, the necessity of resorting to taxation is increased." Such a sentence as this could not have been written except by one who had turned his back squarely upon the policy of war taxation. It regards taxes as a last resort, to be employed only when the public credit shall have been exhausted; the tax policy, on the other hand, holds loans in reserve to be used only in presence of the greatest stress.

But did the views of Congress coincide with those of the Secretary? In one particular only do we find them at variance. Mr. Gallatin desired the new loans to rest upon a permanent revenue sufficient to pay current interest, but the members of Congress had no such view of this necessity as to lead them to press to legalization the necessary bills. It was decided by the Committee of Ways and Means that a war of four years' duration could be carried on for $50,000,000, and in February, 1812, a loan of $11,000,000 was authorized as the sum needed for the first year. Upon the same day that the House passed the loan bill, Mr. Bacon, chairman of the Committee of Ways and Means, made a report in which he advocated "war-taxes," setting forth in a clear manner the policy of the administration. This committee was as yet under the control of Mr. Gallatin. The speech which attended this report is peculiar, showing as it does the excessive and absurd confidence which the extreme war party had in war-loans. After stating that a loan of $11,000,000 was regarded as sufficient for the first year, he said:

It is assumed by the committee that extraordinary or war expenditure of the two succeeding years shall also rest upon further loans; and it is supposed that revenue sufficient to pay only the ordinary expenses and the interest on the old debt and on new loans shall be immediately provided for by the government.[2]

That which is peculiar in Mr. Bacon's speech is his

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[1] "Writings of Gallatin," vol. i, p. 514.

[2] "Annals of Congress," for Twelfth Congress, 1st Session, col. 1095.

warning to Congress against relying upon the proceeds of loans to pay the interest upon debts contracted.

If we suffer ourselves [he said] to yield to the new theory of borrowing both principal and interest, we have no data by which to judge upon what probable terms loans may be obtained at all, or how long it will be before we must wind up business.[1]

Still the temper of the House called for just such arguments, for there was a strong faction that held taxes for the payment of current interest to be superfluous. "How are the exigencies of the government for the next year to be supplied?" exclaimed Mr. Cheeves, who was spokesman for this faction. "Is the deficiency to be derived from taxes? No, I will tell gentlemen who are opposed to them, for their comfort, that there will be no taxes imposed for the next year." And yet in the expenditures for the next year it was necessary to include the interest upon loans already voted. There can be no question but that the financial policy adopted at the beginning of the war of 1812 looked to credit, rather than taxes, as the source of all extraordinary expenditure.[2] Let us then inquire respecting the results of this endeavor to realize the loan policy.

It is not my purpose to trace in detail the course of financial management for the war of 1812. All that is essential to the end held in view may be succinctly presented by a few comments upon the two tables that follow. In these tables will be found certain facts pertaining to the employment of public credit, whether in the form of direct loans or of an issue of treasury notes; the amounts author-

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1 "Annals of Congress," for Twelfth Congress, 1st Session, col. 1098.

2 It is indeed amusing to notice the spleen with which the extreme war party opposed even the moderate proposals of Mr. Bacon for taxation. "At the last session," exclaimed Mr. Wright, of Maryland, "when the question for rechartering the odious British bank was before us, we had to encounter the influence of the Secretary of the Treasury. . . . Now, at this session, he has told us that, if we had a national bank, we should have no occasion to resort to internal taxes; thereby calling the American people to review the conduct of their representatives in not continuing that bank, and thereby to fix the odium of these odious taxes on the National Legislature. Now a system of taxes is presented truly odious, in my opinion, to the people, to disgust them with their representatives and to chill the war spirit. . . . Sir, is there anything of originality in his (Mr. Gallatin's) system? No! it is treading in the muddy footsteps of his official predecessors, in attempting to strap around the necks of the people this odious system of taxation," etc.

ized by the several acts, the amounts issued, and the conditions of their sale, will show quite clearly the degree of success that attended the administration of the loan policy. It is necessary to observe that war was declared upon June 18, 1812, and that the news of a definite treaty of peace arrived in New York upon February 13, 1815. The period covered by the tables, therefore, pertains to those financial measures considered by Congress in view of a continuance of the war, as well as to the employment of public credit for war purposes.

Table A.—*Showing loans authorized, and the facts concerning their sale, for the war of 1812.*

Date of loans authorized.	Amounts authorized.	Amounts issued.	Rate of interest.	Rate of sale.	Rate of sale estimated on gold basis.
March 14, 1812.....	$11,000,000	$10,284,700.00	6 %	par.	par.
February 8, 1813....	16,000,000	18,109,377.43	6 %	88	88
August 2, 1813.....	7,500,000	8,498,581.95	6 %	88½	88½
		9,919,476.25	6 %	80	80
March 24, 1814.....	25,000,000	5,384,138.87	6 %	80	70
		746,403.81	6 %	80–95	65–69
November 15, 1814..	3,000,000	[1] 1,450,000.00	6 %, 7 %	par.	81–89
January 9, 1815.....	6,000,000	200,000.00	6 %	par.	89

Table B.—*Showing treasury notes authorized, and the facts concerning their sale, for the war of 1812.*

Date of acts authorizing Treasury notes.	Amounts authorized.	Amounts issued.	Rate of interest.	Rate of sale.	Rate of sale estimated on gold basis.
June 30, 1812......	$5,000,000	$5,000,000	5⅖ %	par.	par.
February 25, 1813..	5,000,000	5,000,000	5⅖ %	par.	par.
March 4, 1814......	10,000,000	10,000,000	5⅖ %	par.	84–91
December 26, 1814..	10,500,000	8,318,400	5⅖ %	par.	86–90
February 24, 1815...	25,000,000	17,432,780	6 %, 7 %	100–104	82–90

One of the most significant facts which a comparison of these two tables presents, is the relation that seems to

[1] No stock was actually issued, but this sum was borrowed from the banks.

exist between loans and treasury notes. As the power of Congress to secure money by the sale of bonds decreased, reliance upon treasury notes increased. The inability of the government to place bonds was recognized in the latter part of 1814: in December of that year and February the year following, $35,500,000 of treasury notes were authorized. Turning now to a consideration of the loans proper, the record of events shows that the first loan met with no enthusiasm. Although $11,000,000 had been authorized, and the Secretary was anxious that subscriptions should be rapid and sufficient to absorb the entire sum, he found at the end of two months that only $6,000,000 of the stock had been subscribed. Mr. Gallatin admitted that the success of the loan was "more than doubtful," and it was because of the tardy sale of bonds that Congress authorized the first issue of treasury notes. It is true that the terms of this first loan were not attractive, and that the greatest enthusiasm for the war was found outside the moneyed classes; but one must not lose sight of the fact that the only new taxes levied for the support of this loan consisted in a slight alteration of tonnage rates and a tardy increase of customs duties. The financial policy upon which this war was to be carried through appears to have shown signs of weakness before the struggle had been fairly begun.

On February 8th, the following year, the government again came upon the market for money, this time demanding $16,000,000. The weakness of the previous loan was charged to the fact that too strict conditions had been imposed upon the administration in its negotiations; in this loan, therefore, as in all subsequent loans, the only condition insisted on by Congress was the right of reimbursement after a specified term of years. The passage of this act elicited much discussion, concerning both the propriety of the war and the adequacy of the financial policy. Some few members saw that loans resting on good intentions only must lead to disaster.

In finance [said one member] the wisdom of man has never been able to discover any effectual security to public credit short

of certain funds or revenue pledged for the redemption, and sufficiently productive to pay at least the interest, of the debt.[1]

Oddly enough, Steuart on "Political Œconomy" was quoted in support of this common-sense remark. But common sense does not seem to have been regarded at this time as essential to the guidance of the nation's finances, and no steps were taken toward an increase of taxation. This loan was placed at eighty-eight cents on the dollar, while pressing demands were met by an additional issue of $5,000,000 in treasury notes.

Still there are many expressions which show that Congress was beginning to suspect the inadequacy of the loan policy, and at an extra session, called in May, 1813, steps were taken toward laying the foundation of a system of internal revenue. But it would be an error to suppose that the original loan policy was at this time abandoned. Congress had now reached the position defined in Gallatin's financial reports, and recognized the necessity of providing some basis for the credit of the state. There is but the slightest suggestion in the report of Mr. Jones, who was then acting as Secretary of the Treasury, which looked to the employment of taxes for making headway against war demands. According to his view, the chief benefit of new taxes would accrue in enabling the government to carry out its loan policy.

> As reliance [he says] must be had upon a loan, for the war expenses of the year 1814, the laying of the internal taxes may be considered, with a view to that object, as essentially necessary: in the first place, to facilitate the obtaining of the loan; and secondly, for procuring it on favorable terms.

From the message of the President, also, may one learn that the difficulty of negotiating bonds at par was regarded as the only justification of new taxes. The revenue system, as adopted, included a direct tax upon the several States, and internal duties of various sorts. They were called "war-taxes," and, by the act that authorized them, were limited to one year from the conclusion of a treaty of peace. The adoption of this system, however,

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1 "Annals of Congress," for Twelfth Congress, 2d session, col. 896.

When the Lord Mayor of London spoke on the War Loan in Trafalgar Square tens of thousands came to emphasize their loyalty. The Nelson monument in the left foreground is almost covered with painted signs urging the people to subscribe. The subscription amounted to over $5,000,000,000.

appears to have had little influence upon public credit, partly because the new source of revenue could not be relied upon for at least a year, but more especially because the new taxes were temporary, and not co-existent with the debts assigned to them.

This plan of carrying on the war by the proceeds of loans may be said to have broken down in connection with the $25,000,000 loan of 1814. To measure adequately the magnitude of this operation, it must be taken in connection with the $10,000,000 of treasury notes authorized about the same time, from which it appears that $35,000,000 of debt were created by Congress to cover the appropriations of a single sitting. This was a sum equal to five times the average peace expenditure, and to the total *ante bellum* revenue for two and a half years; and it was thought that this sum might safely rest upon the modest appeal to tax contributions just mentioned.

There is one element of complication that must not be overlooked, if the danger and uncertainty which attended the financial operations of this period are to be clearly perceived. Mr. Gallatin had relied largely for the success of his plan, as presented in 1807, upon the assistance of the United States Bank. He thought to control the circulating medium of the country by means of this institution, and to procure from it much assistance in the placement of public bonds. Nor can it be doubted that Congress, in refusing to grant a renewal of the charter of the bank, is largely responsibie for the financial straits into which the government fell. The increase in the circulation of the private banks brought with it the evils of inflation, even before the suspension of specie payments, which occurred in August and September, 1814. Some conception of the difficulty of carrying through any financial operation may be gained when one learns that the government was obliged to select ninety-four State banks as the depositories of its funds; and, so various were the kinds of paper money in use, that it was found necessary to keep four separate ledger accounts in each. This can not, however, be urged as an adequate excuse for the failure of that financial policy adopted for the prosecution of the war. All

that may be truthfully said is, that the failure of this policy was demonstrated more quickly than would have been the case could specie payments and clear accounts have been maintained.

From the table given on page 62, it appears that the proceeds of the loan of March 24, 1814, are presented in three separate sets of figures. This method is adopted in order that the tendencies making their appearance at this time in connection with treasury management may be more perfectly disclosed. There was authorized by this act a placement of $25,000,000 of bonds. The first call was for $10,000,000, which resulted in the receipt of $7,935,581 in cash, and in the issue of $9,919,476 in six-per-cent stock. This, it will be observed, was a sale of bonds at twenty per cent discount, being a lower price by eight cents in the dollar than any which the government had previously accepted. Four months later, a second advertisement appeared calling for $6,000,000 additional of the $25,000,000 authorized. The amount of debt created by this operation was $5,384,134, but the equivalent of cash received into the treasury was only $4,307,307. At the time, however, that the major part of this loan was negotiated, a depreciated paper was accepted as the medium of payment; and, if one permit this discount to modify his calculations, he will discover that the specie price of these bonds was a trifle above seventy cents on the dollar. Nor do these figures adequately present the decadence of public credit, for the government found it necessary to resort to unusual devices in order to place the bonds at all. To the extent of $1,900,000 this debt found subscribers in the cities of New York, Philadelphia, and Baltimore, on condition that the amounts subscribed should be expended in the defense of the cities furnishing the money. Such dickering and trading show the exhausted condition of public credit even more clearly than the discount suffered.

The third attempt to raise money on authority of the act of March 24th marks the collapse of the loan policy. Of the total amount of debt authorized, there remained $12,757,112 to be placed, and we may be sure that the government would have gladly received the en-

tire sum. The amount of stock created was $746,403, the equivalent of cash received being $652,534. The nominal price varied from eighty to ninety-five, the specie price ranging from sixty-five to sixty-nine. Of the moneys thus received, less than $234,000 were available for war purposes, the remainder being paid after the declaration of peace; and of this modest sum $150,000 was signed by certain corporations of Baltimore to build a frigate for the defense of their own harbor. During the last quarter of the year 1814, receipts from all sources fell far short of expenditures, so that an actual deficit of $3,800,000 made its appearance in public accounts.

Do not such facts justify the conclusion that the control of the public treasury during the war of 1812 proved a failure? At the beginning of the struggle, Mr. Bacon said he did not know how long it would be before the treasury must "wind up business;" the course of events showed that it was possible to run on baseless promises a little over two years. But it may be asked: Was this failure due to the erroneous principles upon which the financial policy was based, or to bad administration? The testimony of contemporary statesmen upon this point is of much importance. In the latter part of 1814, the necessity for new and vigorous revenue legislation came to be quite generally recognized. The President stated this as one of the two reasons for calling an extra session of Congress in September. But the most direct and complete testimony upon this point is found in the financial documents of Mr. Dallas, who was called to administer the Department of the Treasury. "The plan of finance," says the new Secretary, referring to the months in question, "which was predicated upon the theory of defraying the extraordinary expenses of the war by successive loans, had already become inoperative." Nor did the new Secretary shrink from placing the responsibility of failure where it belonged. The falling off of revenue and the collapse of credit were not ascribed by him to either "the want of resources or the want of integrity in the nation," but "to the inadequacy of our system of tax-

ation to form a foundation of public credit, and the absence from our system of the means which are the best adapted to anticipate, collect, and distribute the public revenue." He proposed the adoption of a new plan of finance, the characterizing feature of which should be "prompt and resolute application to the resources of the country." In addition to the re-establishment of a national bank, his policy embraced three distinct revenue measures. He demanded, first, war-taxes, nor did he mean by this expression what Mr. Bacon meant in 1812; second, tax-loans, or temporary loans, by means of which the new taxes could become immediately available; third, an extensive use of treasury notes, approaching a little more nearly our modern idea of legal tenders.[1]

Any criticism upon this plan should be made in view of the fact that two years of inadequate financial administration had bequeathed a legacy of confusion and of disordered credit. The problem presented to Mr. Dallas did not consist in forming a war policy which should harmonize in all particulars with the requirements of sound finance, but in rescuing the finances of the state from disaster already experienced. So far as his plan refers to taxes, it is commendable. Twenty-one millions were to be drawn from this source. The tax-loans, also, were demanded by the necessities of the case. It is likewise commendable that he did not at this time make the treasury notes a legal tender for the payment of debts. Yet this would have been the necessary and logical result of the financial policy framed by Gallatin. They who defend the loan policy always assume that public credit can be maintained by an increase of the tax-levy equal to the current demands of the public stock created, but this is found to be a mistake. It is because this is impossible, and because men will not freely lend, that the government feels justified in forcing a loan out of the people by means

1 This financial plan, submitted by Secretary Dallas, may be found in a letter of October 17, 1814, addressed to the Committee of Ways and Means. The note from the committee, asking for suggestions, is also significant. Its first sentence is as follows: "The Committee of Ways and Means have had under their consideration the support of public credit by a system of taxation more extended than the one hitherto adopted." Cf. "Life and Writings of Dallas," pp. 234-243.

of legal-tender notes. The first issue of treasury notes, it will be remembered, was regarded as necessary because of the tardy sale of bonds, and it is but another step in the path already entered upon to give notes a forced circulation. Legal-tender notes lie as a germ in the loan policy, and it is probable that the termination of the war saved the country from the calamity which their issue would have occasioned.

Some of my readers may be inclined to excuse Mr. Gallatin from all responsibility, and to deny that the failure of treasury administration during the war of 1812 argues aught against the sufficiency of the loan policy proposed by him, because Congress refused to grant the new taxes asked for at the beginning of the war. It is true that a proper administration of the loan policy demands clear revenue equal to the debt service and the peace expenditure. It is also true that the special tax-bills recommended to the Twelfth Congress failed to secure legal sanction; but it would be incorrect to conclude, because these particular taxes were withheld, that the essential requirements of the loan policy were not complied with. A glance at the general balance-sheet covering the three years of the war will show that permanent revenue not only covered permanent expenditure, but furnished a surplus of nearly $6,000,000 for war purposes. Although the new taxes were refused, the receipts from old taxes exceeded expectation; it is impossible, therefore, for the advocates of the loan theory to shift the responsibility of the failure of Mr. Gallatin's policy upon the shoulders of Congress. This balance-sheet is presented in the following table:

Table showing the source of moneys expended for war purposes.

YEAR ENDING	War expenditure paid out of proceeds of taxes.	War expenditure paid out of proceeds of loans.
December 31, 1812........	$3,560,150.00	$12,477,988.39
December 31, 1813........	1,399,277.71	24,849,810.41
December 31, 1814........	775,828.53	27,047,309.37 [1]
Total................	$5,735,256.24	$64,375,108.17

[1] There is included in this sum an actual deficit in accounts.

It thus appears that, for a total war expenditure of some $70,000,000, it was found necessary to create a debt of only $64,300,000, a fact which shows how futile is an apology like that suggested above in favor of the loan policy. So far as clear revenue is concerned, the demands of the theory were met, and it is the theory rather than the remissness of Congress that must be held responsible.

Or, again, it may be that some one, quoting that old maxim, *salus populi suprema lex*, a maxim regarded by dullards as the first principle in finance, will ask: Wherein did this policy fail? Did not the Government get the money and carry through the war? Such a question can only be answered by placing the actual results of treasury management during the war of 1812 in comparison with the demands of adequate management.

An adequate financial policy will place the credit of a state on so firm a basis, and guard it so jealously, that the government will never be called upon to suffer ruinous discount in the placement of its bonds. The record of this war shows that even at the beginning there was no enthusiasm for the public stocks, that every month as it passed saw the nation's credit decline, and that the last quarter of the year 1814 showed a deficit in public accounts while the government still possessed the right to borrow $12,000,000.

An adequate financial policy will provide such extensive resources that a war once entered upon may be carried through to the end without change of plan. It must be elastic and pliable, so as to be ready for all probable emergencies. In the present instance, after little more than two years of vain endeavor to supply the demands of the government, the original plan was abandoned, and a new theory was admitted by the administration and by Congress. The evils necessarily attendant upon this change in the midst of a war were only obviated by the return of peace.

An adequate financial policy will not be forced to use treasury notes, except as a convenient method

of managing its taxing system. We have already noticed how that unwarranted interference with the circulating medium follows logically from a determination to throw the entire weight of war expenditure upon public credit.

It must be admitted that Mr. Dallas passed lightly over this stupendous failure in financial administration when, in reviewing the financial operations of the war, he said:

> An increase of the expense, and a diminution of the supply, must have been anticipated as the inevitable consequences of that event; but the government reposed with confidence for all the requisite support upon the untried resources of the nation in credit, in capital, and in industry. The confidence was justly reposed; yet it may, perhaps, be considered as the subject for regret, and it certainly furnishes a lesson of practical policy, that there existed no system by which the internal resources of the country could be brought at once into action, when the resources of its external commerce became incompetent to answer the exigencies of the time. The existence of such a system would probably have invigorated the early movements of the war, might have preserved the public credit unimpaired, and would have rendered the pecuniary contributions of the people more equal as well as more effective. But, owing to the want of such a system, a sudden, and an almost exclusive, resort to the public credit was necessarily adopted as the chief instrument of finance. The nature of the instrument employed was soon developed; and it was found that public credit could only be durably maintained upon the broad foundations of public revenue.[1]

It is not my purpose to follow thus in detail the financial history of the war of 1861. So far as principles are concerned, it presents nothing with which the foregoing study has not already made us familiar. Here is found the same policy for the management of the public treasury; this policy follows the same course in its development, and works the same general results. The only variation in the record pertains to the use of treasury notes, for, in the case of this second war, the loan policy was not arrested until these notes were given the legal power of paying private debts. Upon the main point there can be no question. The plan recommended by Secretary Chase, and adopted by Congress, was to rely upon public credit for carrying

[1] "Report on the Finances," December, 1815.

through the war. In a special report of July, 1861, which deals with ways and means, the Secretary expresses himself as follows:

To provide the large sums required for ordinary expenditure, and by the existing emergency, it is quite apparent that duties on imports, the chief resource for ordinary disbursements, will not be adequate. The deficiencies of revenue, whether from imports or other sources, must necessarily be supplied from loans; and the problem to be solved is that of so proportioning the former to the latter, and so adjusting the details of both, that the whole amount needed may be obtained with certainty, with due economy, with the least possible inconvenience, and with the greatest possible incidental benefit to the people.

The Secretary has given to this important subject the best consideration which the urgency of varied public duties has allowed, and now submits to the consideration of Congress, with great deference and no little distrust of his own judgment, the conclusions at which he has arrived.

He is of the opinion that not less than eighty millions of dollars should be provided by taxation, and that two hundred and forty millions should be sought through loans.

It will hardly be disputed that, in every sound system of finance, adequate provision by taxation for the prompt discharge of all ordinary demands, for the punctual payment of the interest on loans, and for the creation of a gradually increasing fund for the redemption of the principal, is indispensable. Public credit can only be supported by public faith, and public faith can only be maintained by an economical, energetic, and prudent administration of public affairs, and by the prompt and punctual fulfillment of every public obligation.[1]

This financial policy may be more clearly apprehended if we notice the estimates presented by the Secretary. As has been already stated, he proposed to raise $80,000,000 by taxes, as against $240,000,000 by loans. Of this amount of clear revenue, $65,800,000 were required to meet the ordinary expenditures of the peace establishment. It was believed that existing laws would provide about $60,000,000, from which it followed that new taxes to the amount of $20,000,000 were required. Of this sum, $9,000,000 were to be devoted to payment of interest upon the new debt, and $5,000,000 to the establishment of a sinking-fund for its final expungement. Such was the financial plan upon which this great war was begun.

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[1] "Report on the Finances," July 4, 1861.

The revenue law which followed this report modified customs duties so as to intensify the principle of industrial protection, established a three-per-cent income-tax upon all incomes over $800, and apportioned a direct tax of $20,000,000 among the several States. The income-tax was not to take effect until January, 1862, and, as the direct tax was apportioned to the South as well as to the North, the treasury could not hope for the entire amount levied.

In the December report, 1861, the Secretary declared renewed confidence in the financial plan which he had previously presented. It was found, however, that receipts from customs and from the sale of public lands had fallen off. Thus, for the quarter ending September 30th, customs duties had yielded but $7,198,602. For the calendar year ending 1861, the government received but $30,795,795 from this source, as opposed to $50,747,990 in 1860, and $53,800,596 in 1859. There seemed, therefore, just ground for apprehension lest existing taxes should fail to support the peace establishment, and the loans which the government chose to place. This fear of a deficit, from ordinary sources of revenue, impressed itself upon the mind of the Secretary, and, in consequence, he proposed additional duties on tea, coffee, and sugar; a modification of the income-tax, so as to render it more productive; an increase of the direct tax to the States; and a tax on whiskies, tobacco, bank-notes, instruments of conveyance, and the like; in short, he proposed the establishment of the system of internal duties. Now, all this has the appearance of an abandonment of the loan-policy, and the adoption of the policy of carrying through the war by taxes, but this is true in appearance only. The total sum of clear revenue hoped for from all these sources of income was but $90,000,000, and this, as the Secretary said, was not more than enough to meet "even economized disbursements, and pay the interest on the public debt, and provide a sinking-fund for the gradual reduction of its principal." "It will be seen at a glance," says the report in another place, "that the amount to be derived from taxes forms but a small portion of the sums required for the expenses of

the war. For the rest, reliance must be placed on loans." It is also worthy of notice, as throwing additional light upon the policy of the administration, that the mind of the Secretary seems at this time to have been taken up with his scheme for establishing a system of national banking; for, as is well known, one purpose of this scheme was to provide a ready market for public bonds. It comes, therefore, into perfect harmony with the loan policy already adopted.

It was in the latter part of the year 1863, and during the first part of 1864, that the inadequacy of the loan policy as a basis of war-financiering forced itself upon the minds of those who managed public affairs. "To check the increase of debt," says the report of 1863, "must be, in our circumstances, a prominent object of patriotic solicitude." And again: "Hitherto the expenses of the war have been defrayed by loans to an extent which nothing but the expectation of its speedy termination could fully warrant." The report then restated the financial policy as adopted in 1861, and continued:

> The financial administration of the first fiscal year after the outbreak of the rebellion was conducted upon these ideas. The acts of Congress at the extra session of July, 1861, were framed with the intention of supplying the full amount of revenue demanded by them. But receipts disappointed expectation, and it soon became obvious that a much larger proportion of the means needed for the fiscal year 1862 than the principle adopted would allow must be derived from loans.

But the most interesting expression in this document pertains to the estimates for probable future demands:

> These statements [says the Secretary, referring to the estimates] illustrate the great importance of providing, beyond all contingency, for ordinary expenditures and interest on debt, and for the largest possible amount of extraordinary expenditures, by taxation. In proportion to the amount raised above the necessary sums for ordinary demands will be the diminution of debt, the diminution of interest, and the improvement of credit. It is hardly too much—perhaps hardly enough—to say that every dollar raised for extraordinary expenditures or reduction of debt is worth two in the increased value of national securities, and increased facilities for the negotiation of indispensable loans.

Could this truth have been recognized at the beginning of the war, and could it at that time have influenced the treasury policy, the financial history of the last twenty-five years would have been materially modified.

Congress also, in the latter part of 1863, began to recognize the essential weakness of the loan policy, and to turn its attention to the necessity of taxes for distinctively war purposes. The great tax-bills of the war were those of June, 1864. Mr. Morrill, in whose speech of a year before there were statements showing that the original policy was yet intact, admitted, while presenting these new bills, that money must now be secured by every possible means:

> The treasury [he said] requires a larger supply of means, and such sources of revenue as have not already yielded their maximum contributions must now be sought, so that we may fill the measure of our wants. . . . This [bill] is intended as a war measure, a temporary measure, and it is needful that it pass speedily. Every day's delay in the passage of this and the internal revenue bill costs the treasury not less than $500,000.[1]

This language is very different from the financial dilettanteism that marked the attitude of our financiers during the first two years of the war.

It is somewhat difficult to exhibit accurately the rapid fall of public credit from 1861 to 1866; but I have undertaken in the following statement to approximate such an exhibit by showing the specie price of all the obligations issued during the war. The computation has been made by estimating the value of the total receipts from credit for each quarter at the average price of gold during that quarter. The only source of error in this method arises from the fact that the average price of gold for any three months may not be the actual price at which the proceeds of bonds were covered into the treasury, but any closer computation requires more complete data than the authorities at Washington have yet given. It is, however, believed that the conclusions may be relied upon as substantially correct.

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[1] Young's "Customs-Tariff Legislation," p. cxxxiii.

Table showing treasury receipts, from public obligations of all sorts, for each quarter during the war, and the gold value of such receipts, estimated on the average price of gold for each quarter.

SUMMARY.	Gross receipts from debt created.	Gold value of gross receipts.	Percentage realized.
For the quarters ending—			
March 31, 1862......	$60,947,202.67	$59,527,132.84	97·67
June 30, "	209,049,203.81	200,230,763.59	95·78
September 30, "	68,934,420.36	59,648,953.94	86·54
December 31, "	131,631,479.40	101,250,933.95	76·92
March 31, 1863......	178,569,759.25	115,195,351.69	64·51
June 30, "	216,460,067.49	145,829,147.47	67·37
September 30, "	118,267,491.75	89,800,506.48	75·93
December 31, "	150,450,843.85	100,862,245.72	67·40
March 31, 1864......	191,922,104.42	120,220,006.20	62·64
June 30, "	235,371,791.92	122,581,629.23	52·08
September 30, "	147,735,822.42	61,295,592.72	41·49
December 31, "	179,908,674.29	80,365,201.80	44·67
March 31, 1865......	175,313,376.72	88,094,971.80	50·25
June 30, "	361,905,625.74	253,406,319.14	70·02
September 30, "	138,765,727.22	97,038,873.04	69·93
For the years ending—			
December 31, 1862.....	$470,562,306.24	$420,657,784.32	89·39
" 31, 1863.....	663,748,162.34	451,687,251.36	68·05
" 31, 1864.....	754,938,393.05	384,432,432.95	50·93
September 30, 1865.....	675,984,729.68	438,540,163.98	64·87
For the forty-five months of the war..............	$2,565,233,591.31	$1,695,347,632.61	66·09

It seems superfluous to comment on such figures as these. A treasury administration that permits the credit of a wealthy people to decline so that its obligations fall fifty per cent and remain there for a year, can hardly be called successful. Yet the results here displayed, as also the forced circulation of treasury notes, follow naturally from the attempt to carry through a war by loans.

But the lesson of these public accounts is not fully appreciated until it is observed with what ease a system of internal revenue may be made to respond to a vigorous and decided administration, for this shows how unnecessary it is to rely wholly upon public credit for extraordinary expenditures. In this connection the following table is pertinent for our consideration.

Table showing receipts from various sources, for fiscal years, in denominations of millions.

	1861.	1862.	1863.	1864.	1865.	1866.
Customs revenue.....	39·6	49·0	69·0	102·3	84·9	179·0
Internal revenue.....	....	1·7	39·1	110·2	210·6	311·2
Miscellaneous........	1·9	1·1	4·5	52·1	38·2	67·8
Clear revenue......	41·5	51·9	112·6	264·6	333·7	558·0
From loans........	23·7	433·6	595·6	696·0	864·8	92·6
Total revenue....	65·2	485·5	708·2	960·6	1,198·5	650·6

It requires no extended study to discover the meaning of these figures. The criticism which they offer makes its appearance when one asks what would probably have been the financial consequences could the receipts from internal revenue have been moved ahead two years. Suppose, for example, that Secretary Chase could have received from this source $110,000,000 in 1862, $210,000,000 in 1863, and $311,000,000 in 1864; what a change would it have produced upon the course of financial administration! Its moral effect upon the South, working especially through her European sympathizers, would have brought the war to a more speedy termination, the credit of the government could not have suffered as it did, while the advocates of legal-tender money would have been deprived of the argument of necessity. Now the responsibility for the tardy flow of revenue from internal duties is traceable to the policy upon which the finances of the war were set on foot, and not to the inability or the reluctance of the country to pay. Secretary Chase denied the necessity of meeting any part of war expenditure from war-taxes, because the financial theory which he espoused deprecated the endeavor; and it required nearly three years of disastrous treasury management to convert the administration and Congress from this erroneous theory. In view of actual conditions, it is perhaps a little extravagant to suppose that the receipts from internal revenue could have been moved ahead two years, but it is altogether reasonable to conclude that a vigorous administration might have anticipated actual results by eighteen months.

This estimate allows nearly a year for the establishment of the system, and claims only that internal revenue should have begun to come into the treasury at the rate of $9,000,000 a month as early as July, 1862. And when it is noticed how quickly the industries of the country responded to the laws of 1864, as shown by the receipts for the year 1865, one can not regard this claim as at all impracticable. There is here disclosed the fundamental error of that theory which looks to credit as the only source of war expenditures. It is blindly optimistic, and so deprecates an appeal to sources of revenue that might with ease be opened. They who undertake its administration are sure to let matters drift until financial disaster awakens them to the fact that the financial problem is no longer under their control. This theory springs from financial ignorance, from a sense of administrative weakness, and from a thorough distrust of the people.

It appears, then, that the history of the war of 1861, like that of 1812, bears direct testimony against the sufficiency of the loan policy. It is no apology for the men who administered public affairs that they looked upon the Rebellion as a local insurrection, for, in matters of public financiering, revenue must conform to necessary expenditure; and no policy can meet approval which fails to supply all the money that is needed for as long a time as it is needed.

What is the true plan for the financial management of a war?

Thus far our argument has proceeded according to the logic of exclusion. We have learned that the tax policy does not conform to well-known principles of human nature, and that the loan policy fails to bear the test when tried; but since taxes and loans are the only sources of revenue open to modern financiers, it follows that the true policy must embrace them both. Our further study, therefore, must concern itself with inquiring what constitutes a reasonable union of taxes and loans.

We shall be assisted in answering this question if we notice, at the outset, certain fiscal principles or truths that

point to the correct theory of treasury management. First, the habit of bearing taxes is one easily acquired, if only the instruction be given in a proper manner. It is never necessary to depend altogether upon loans for war expenditure, and the administration that shrinks from a levy of taxes, lest the war spirit be chilled, shows either a doubtful cause or a weak-kneed cabinet. As a second principle may be stated the fact that it is easier to raise the rate of existing taxes than to establish a new system of duties. From this it follows that the germ of a war policy lies back in the treasury policy of ordinary times. Again, it is popular support, rather than the adherence of a syndicate of banks, which insures the success of a financial policy. This is true, because popular sentiment in favor of the administration guarantees the support of the banks, but it is not true that the support of the banks brings with it general enthusiasm. This does not mean that banks should never be employed as agents of the government, but that the administration should be superior to the criticisms of the banking interest, that the basis of its operations should be as broad as possible, and that it is no sign of weakness to appeal to patriotism as a motive for lending money. **And, lastly, it is a truth worth remembering that democratic peoples are willing to go all lengths with a government which takes them into its confidence. It is assumed that the purpose of the war is approved, otherwise there is no apology for undertaking it; but, granting this, personal sacrifice and assistance are assured to a government so long as the public continues to have confidence in the efficiency of its administration.** The meaning of this fact is, that an adequate financial policy should be bold, courageous, sufficient, and simple; that it should lie close to the sympathies of the people, and not fear to make from them searching demands. We have now before us the raw material out of which to construct a plan for the financial management of a war.

Coming then directly to the question in hand, it is of prime necessity to recognize that good financiering in

times of emergency is only possible upon the basis of an adequate revenue system previously established. It has been already stated that some preparation in time of peace should be made against the advent of war, but that the assignment of a particular tax to this purpose, or the accumulation of a war-reserve, does not accord with the most perfect financial requirements. How, then, may the peace establishment provide against unusual demands? Nothing more is required for this purpose than that the permanent system should be so adjusted as to respond quickly to any change in rates imposed, and this can be easily done by fixing the ordinary rate of taxation below the maximum revenue rate. But, if the actual rate of taxation in ordinary times be at or above the maximum revenue rate, the administration can hope for no assistance, in case of an emergency, from established taxes. Under such circumstances the government is embarrassed at the outset, and easily persuades itself that an appeal to credit is the only method for making headway against demands. But let it be supposed, on the other hand, that the country possesses a broad system of taxation, so that ordinary demands may be met by imposing light duties, any embarrassment encountered by the minister of finance at the beginning of a war must be of his own making.

But, assuming such provisionary measures to have been taken, what is the next step in an adequate war policy?[1]

Our answer may be given without hesitation. New sources of revenue must be opened by the levy of new taxes. But, it may be asked, is not such a proposal a virtual abandonment of the loan policy? This can not be admitted; for it is essential that a law should be passed to provide for clear revenue, in addition to that secured by raising the rate upon existing taxes, before a financier has any right to assume that he can borrow large sums without

[1] Were this question asked for the United States, the answer might be given more explicitly. In view of the peculiar relation existing between the Federal government and the several States, there are many reasons for saying that this first tax should be a direct tax upon the States, apportioned and collected on the principle of "revolutionary requisitions."

The Most Popular French War Loan Poster

depressing public credit. He can not rely entirely upon the new revenue derived from the old taxes, because this revenue is not co-existent with the debts created. A true financial policy, also, must hold in view the termination of the war as well as its continuance, and do nothing which can in any manner obstruct the speedy reduction in the rate of permanent taxes upon a return of peace. For, if the extraordinary income from the permanent taxes be mortgaged to the support of a permanent debt, the first claim of a good revenue system is disregarded. The elastic quality of the system would be thereby destroyed, and the country would be poorly prepared to meet another fiscal emergency. And it must be further noticed that these new taxes, once established and brought into running order, are ready at hand to assist in the expungement of debts when the war shall have terminated. It thus appears that the new taxes tend to strengthen public credit, even before they become remunerative; they relieve the temporary revenue derived from permanent taxes, so that it may again serve as the temporary basis of new loans; and they assume the whole weight of the debt upon a return of peace.

It may be objected to the plan here proposed that, should the struggle prove of slight duration and little cost, the country is burdened with useless taxes; but this objection seems to be made without due consideration. Assuming the difficulty to be quickly terminated, it is more than probable that the strong financial policy adopted by the administration rendered great assistance in attaining so desirable an end. If a destructive war can be obviated by the voting of taxes, there are few who would withhold their assent. Nor is it necessary, in the case assumed, that the taxes should prove an actual burden to the people. New taxes require some considerable time before they become productive, and, should the occasion for them pass away, they may be abolished before taking much from the pockets of the people. Let, then, no financier argue that war-demand will probably be small, and that it may be met by loans without an appeal to taxes; for the administration certainly needs the moral influence of the tax-laws,

the revenue which these laws are capable of bearing may be required, and, if the events show the solicitude of the administration to have been groundless, no great harm is done.

It remains for us to consider what use should be made of public credit, and to discover the principle according to which the extraordinary expenditure should be apportioned between loans and taxes. The theory of public borrowing is very simple. Public credit should always be regarded as a means of anticipating revenue. It is a short cut to capital, and the first great service of loans in time of war is to give the administration immediate control over capital upon the declaration of hostilities. But such borrowing does not necessarily create a permanent debt. It rests, in the first instance, upon the extraordinary receipts arising from the increase of rate in the permanent revenue system. Should the war, however, continue for any considerable time, it would be necessary to convert the debt thus created into a permanent or time debt, and assign it to new funds for support. And here, it may be said, is the only point at which ignorance of the probable duration of the extraordinary demands may be permitted to influence the financial policy of the administration. It is proper, until the future may be forecast with some degree of certainty, that temporary debts rather than permanent debts should be used. And here, too, is disclosed the peculiar service rendered by an elastic revenue system, for the quick command which such a system grants over revenue provides a solid basis of credit at the beginning of a war, and so insures a good price for the first bonds negotiated.

But there is another and more important service that may be rendered by loans. When a government gives bonds in return for capital, the individual who supplies the capital does not feel that sense of personal loss which attends the payment of a tax. He has merely changed the character of his property. It thus appears that by means of loans a government may hope to secure immediate control over large funds of capital while yet allowing the motives for continued industry full liberty of action. So far as it seems necessary to use credit for attaining this

end, the obligations created against the state must run for some considerable time, and be assigned to a reliable fund for the payment of the annual interest which they demand.

In the services here brought to view lies the entire theory of public credit. Loans are always a means of anticipating assured revenue. No other meaning can be attached to them when used to carry through the financial operations of a war, for no system has yet been devised for evading the necessity of extraordinary taxes as the result of extraordinary expenditures. Our general conclusion then is, that sound financial management inclines always toward taxes. The measure of the amount that may be secured by this means is found in their observed effect upon current industry, for the demand for clear revenue must never go so far as to discourage industrial activity.

It is impossible to proceed much further in a general discussion of this subject, for the conflicting interests to be harmonized, and the varying importance of the factors that enter into the problem, must influence greatly the application of the principles suggested. It may, however, be permitted to take one step in the direction of formulating a rule of wide application for the financial conduct of a war, by which the relative use to be made of taxes and loans may be roughly indicated. At the beginning of hostilities, revenue from loans may properly outbalance revenue from taxes, but, as the war progresses and the demands increase, taxes should be continually forced into greater prominence. There are several considerations that favor this rule. Thus the necessity for temporary loans is always greater at the beginning of a war than at any subsequent period. As the newly levied taxes become more and more productive, and as the people become accustomed to high rates of payment, the legitimate use of loans is narrowed. But the most forcible reason favoring the rule is the following: The greatest stress which the advent of a war throws upon industries arises from the necessary re-adjustment of labor to new lines of demand. It is this point which is not duly appreciated by writers upon finance. They do not perceive that the strain upon

a treasury policy comes at the beginning of a war. A condition of war is not a condition of peace from any point of view, and the industrial transition from the one to the other is always attended with danger and may prove the occasion of disaster. But, if the financier can only bridge over this chasm and establish business firmly on a war basis, he may extend his taxing system with as much confidence as if the people were living in a state of profound peace. It is during this period of re-adjustment that public credit renders its greatest service to the administration. At no future time during the continuance of a war can such strong reasons be urged in favor of its employment.

It seems, then, that the theory for the administration of a treasury during the continuance of a war contemplates, first, the formation of a financial policy at the time when hostilities are first declared; and, second, the development of the policy after industries are well adjusted to belligerent conditions. And, as has been set forth in the foregoing analysis, the formation of the policy demands the legalization of three fiscal measures.

1. The rate of taxation in the permanent revenue system must be raised. The new income thus secured will serve as the basis of the first loans, and, when relieved by other funds, may be employed as a contingent fund or as a source of war expenditure. Nothing must be done to endanger the repeal of this measure upon a return of peace.

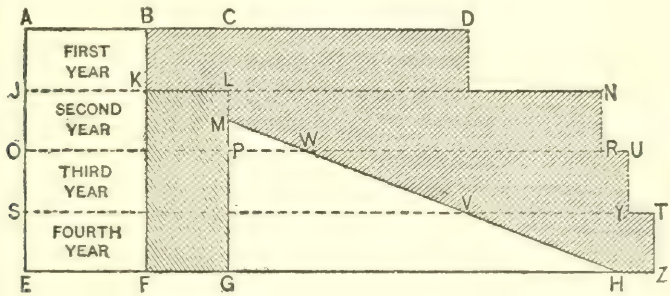
2. New sources of revenue must be opened by the levy of new taxes. The estimated proceeds of these taxes must exceed, if possible, the demands of loans for interest payment. This will assist in maintaining the credit of the state, it will give some revenue for war purposes while hostilities continue, and will provide revenue for the expungement of the debt when the demands for war expenditure shall have ceased.

3. A large loan, equal to the satisfaction of all possible demands, must be authorized, and the minister of

finance must be granted large discretionary powers in its placement. In this manner there is created the machinery for financial operations, and under a strong administration there is little fear of failure.

The principles which control the development of the policy are the same as those which shaped its establishment. If temporary loans were resorted to, they should be funded upon the proceeds of the new taxes as soon as possible. The financier may hope for assistance from his new taxes within eighteen months of their levy, and, if demands continue to expand, his call for clear revenue should be gradually increased until revenue machinery be speeded to its highest productive capacity. But there is a limit to possible war consumption, and, with a gradually increasing income from taxes, clear revenue must eventually overtake any possible demand.

This theory of treasury management may, perhaps, be more clearly apprehended if stated with the assistance of the following diagram:



In this figure the horizontal lines, in the direction from left to right, measure the productivity of revenue machinery, while the perpendicular distance from the top represents the time through which it operates. Thus the line *A B* shows the intensity of the demand made upon the permanent revenue establishment in time of peace, and, since the line *A J* covers one year's time, the parallelogram *A K* represents the normal income for a year. The first measure upon the outbreak of a war should be to increase

the rate imposed upon the peace establishment. Let it then be increased by B C. If, now, the permanent system has been formed according to correct principles, and is elastic in character, this advance in the rate of imposition will yield increased revenue; but, since it is necessary properly to advertise such a change, it is assumed that this addition to clear receipts will not make its appearance till the beginning of the second year. It follows, then, that the entire war demand of the first year must come from loans. This is represented in the figure by the parallelogram K D. There is no danger, however, but that this stock will bear good prices, because it rests upon income assured by revenue machinery already in operation. The fund, which sustains the credit of the government during the second year, is represented by the parallelogram K P, from which it appears that the entire receipts flowing from the permanent establishment during the second year is equal to the parallelogram J P. During the second year, also, the newly established taxes begin to lend their assistance in carrying on financial operations, and the income from this source is represented by the triangle M P W. This revenue is shown as beginning in the middle of the second year, because it will probably take eighteen months to bring an entirely new system into working order. It thus appears that a large share of the extraordinary expenditure of this year also must be secured from loans, which is represented in the diagram by the figure L M W R N. But with the beginning of the third year it may be assumed that the industrial re-adjustment has taken place, and the financier may constantly and persistently extend his demand for clear revenue; and, since there is a limit to war consumption, the necessity of loans decreases with every increase in clear revenue. Thus the total revenue for the third year is represented by the parallelogram O Y, of which clear revenue provides a sum represented by the figure O S V W the remainder being supplied by loans. In the fourth year, of a total expenditure represented by E Z T S, loans are called upon to furnish the comparatively small sum of V H Z T. It lies as an essential part of the treasury policy

here defended that the newly established system of taxation should be continuously expanded until financial exigencies shall have passed away; and this may be brought about either by a return of peace or by the fact that clear revenue has overtaken war demands. It is useless to say that this is impossible: it is perfectly feasible, provided only a strong and vigorous policy be adopted at the beginning of the war. The difficult part of the task imposed upon the financier is during the first and second years of the war. At this time there is demand for wisdom and firmness, for no administration can recover itself if it indulge in weakness and inefficiency at the time when a policy is set on foot.

Our conclusion, then, respecting the appropriate financial policy for the conduct of a war is the following: Reliance can not be placed wholly upon loans nor wholly upon taxes, but fiscal administration should be so adjusted as gradually to change the burden of expenditure from credit to clear income.

PART IV.

Bonds and Taxation

Bonds and Taxation

THE WEALTH OF THE BELLIGERENT NATIONS

In determining upon a policy of national taxation one absolute limit to all calculations must be a country's total taxable income. The table on page 94 gives an approximation to this total in comparative form.

Such figures, however, are subject to important limitations. The matter has been briefly discussed from the point of view of the United States in a recent issue of "The Economic World" of New York, from which we quote the following paragraphs:

"Nobody knows with absolute precision the sum-total, in terms of money, of the annual income of the population of the United States. The most competent estimate, perhaps, is that of Professor W. I. King, who, in his most interesting book, 'The Wealth and Income of the People of the United States,' put it at $30,580,000,000 for the year 1910. Naturally, there has been an increase since 1910; and if the rate of increase shown from 1900 to 1910 has been maintained down to 1917—though this is highly doubtful—the total income of the population of the United States in 1917 should be between $38,000,000,000 and $40,000,000,000. Here, then, is the absolute maximum that could conceivably be drawn upon through taxation to pay the going expense of the war. As has been shown, however, much the largest part of this maximum is unavailable as the subject-matter of direct taxation. To a very moderate extent, indeed, it can almost all be touched by indirect taxation, particularly taxation on the consumption of things in general use, but not absolute necessities of life. The natural limitations upon this kind of taxation, or the results obtained from it, are marked, as the British have discovered. For the increase of taxation reduces the consumption and hence the yield of the tax. Thus heavy increases in the excise duties in Great Britain

in 1916 actually reduced the yield from these taxes for the year by £5,000,000, as compared with the yield in 1915, and brought them £10,000,000 below the sum estimated in the budget as their probable yield.

"That part of the total national income, then, which appertains to the great majority of any population is virtually beyond the reach of severe direct taxation, on political and social grounds; and at the same time comparatively little can be derived from it through indirect taxation. Only a certain remainder of the national income can in effect be subjected to that direct and at the same time quickly operative taxation which will give the huge sums of money in hand required by a government to meet a considerable part of the current cost of a great war. At the same time, it is an all-important question what this remainder may be in the United States, if the plan is to be carried through of paying anything like one-half the current expense of the war with Germany from the proceeds of national taxation.

"We have but two determinate figures upon which to base an estimate of the amount of this remainder. We know from the Federal corporation tax returns for 1915-1916 that the entire amount of the earnings of all the corporations in the United States in that fiscal year was $5,184,442,389. We know also that the sum-total of the 'normal' personal income taxes collected in the same fiscal year was $23,995,777 (though supertaxes brought the grand total of collections up to about $67,760,000). Inasmuch as the 'normal' tax is 1 per cent of the taxable income, we are able to deduce that the aggregate amount of the taxable personal incomes in the country,—*i. e.* those in excess of the statutory exemption limit,—was $2,399,577,700. Of course, if the exemption limit were reduced, say, to $2,000, the sum-total of taxable personal incomes would be considerably increased, perhaps by enough to bring this sum-total up to $5,000,000,000. But, be it remembered, these corporation and personal incomes included all the 'profits' made in the country in 1915-1916, save those smaller than the exemption limit for individuals. The important fact, however, is that we can

count on no other remainder of the total national income, upon which direct war taxation can be imposed, except the sum of the total earnings of our corporations and of the total taxable income of individuals. And this sum is about $7,500,000.000 with the present exemption limit for individual incomes, or, say, $10,000,000,000 with that limit reduced to $2,000. If the war with Germany assumes the guise for us that it has for Great Britain or France, quite one-half of this grand total of taxable income will be required to pay one-half the annual expense we must meet. The effects of so radical a reduction of what may be called the economically effective part of the national income upon the general economy of the country may easily be imagined."

In the subjoined table it will be observed that the wealth of the Entente Allies before the entrance of the United States into their midst is estimated at 244 billions of dollars and their combined national income at 28.5 billions. Their total borrowings are to date 46 billions or 61% above the annual income and represent a mortgage of 18.8% on their total wealth. The wealth of Germany and its Allies is estimated at 134 billions of dollars; their combined income 17 billions and their borrowings $23,630,000,000. The latter item is equivalent to 17.6% of their combined wealth and 39% above their combined income.

With the addition of the United States to the ranks of the Entente, matters are considerably changed. The present national income of the United States is estimated very conservatively at 38 billions of dollars and its wealth at 220 billions. In other words, the resources of the Entente in terms of dollars and cents have been doubled by the action of the United States in taking up the cudgels in behalf of democracy. On the basis of the present borrowings of belligerent nations, it is fairly evident that the United States could borrow without difficulty, as a future mortgage on its wealth, to the extent of 40 billions and could then maintain its financial integrity equally as well as any of the most successful European belligerents.

Population, Wealth, Income and Debts of Belligerent Countries[1]

	Population[2]	Wealth	Income	Borrowings[11]
A. Entente Allies:				
United Kingdom	45,370,530	$80,000,000,000[3]	$10,500,000,000[7]	$19,000,000,000[12]
France	39,601,509	70,000,000,000[4]	6,000,000,000[8]	11,000,000,000
Russia	178,378,800	50,000,000,000	6,500,000,000	13,000,000,000
Italy	36,120,118	25,000,000,000	4,000,000,000	3,000,000,000
Belgium and Serbia	10,335,685	12,000,000,000	1,250,000,000	. . . .[13]
Portugal and Rumania . . .	13,465,994	7,000,000,000	600,000,000	. . . .[13]
United States	102,826,309	220,000,000,000[5]	38,000,000,000[9]	. . . .
Entente Nations	426,098,945	$464,000,000,000	$66,850,000,000	$46,000,000,000
B. Central Powers:				
Germany	64,925,993	$87,000,000,000[6]	$10,500,000,000[10]	$15,500,000,000
Austria-Hungary	49,458,421	40,000,000,000	5,500,000,000	7,000,000,000
Turkey and Bulgaria	25,611,416	7,000,000,000	1,000,000,000	1,130,000,000
Central Nations	139,995,830	$134,000,000,000	$17,000,000,000	$23,630,000,000

[1] While all the figures pertaining to wealth and income are necessarily more or less conjectures, it is believed that for comparative purposes the present figures give a fair view of the situation. If we have erred at all, it has been on the side of conservatism rather than liberality. The most reliable authorities were consulted, though different authorities in the same country often disagree. Even in cases where official statistics are presented, the comparability of the figures may be vitiated by the fact that different standards are used in the process of estimation.

[2] Population statistics refer in every case, except that of the United States, to the latest census enumerations. It was thought that the war mortality might greatly counterbalance any natural increases in the population since the last censuses. The United States figures are the latest estimate of the United States Bureau of the Census.

[3] On the basis of Helfferich's estimates, cf. Karl Helfferich, *Deutchlands Volkswohlstand* 1888-1913, Sixth edition, Berlin 1915, pp. 113-114.

[4] Ibid., p. 113.

[5] Calculated on the basis of figures given in the Statistical Abstract of the United States 1915. Cf. also *Seventh State Conference on Taxation, Report of the Committee on the Relation of State and Federal Taxation*, 1917, Appendix B.

[6] Helfferich, op. cit.

[7] Pierre Leroy-Beaulieu, *Les Impôts et les Revenus en France, en Angleterre et en Allemagne*, Paris 1914, p. 10.

[8] Ibid., p. 7.

[9] On the basis of King's figures, cf. W. I. King, *Wealth and Income of the People of the United States*, New York 1915, p. 129.

[10] Helfferich, passim. Leroy-Beaulieu, op. cit., disagrees with Helfferich. The latter's estimate is about 9 billion dollars.

[11] The figures in this column are based primarily on the excellent summary of war borrowings which appeared in the New York American, January 5 1917—brought up to date.

[12] This figure already embraces the loans to Allies and Dominions.

[13] No figures are here given because they are included in the borrowings of France, Great Britain, etc.

LOANS OF THE BELLIGERENT COUNTRIES

1. United States

On March 31, 1917, the national debt of the United States was composed of the following items:

National Debt, March 31, 1917[1]

Debt bearing no interest (including U. S. notes, national bank notes, federal reserve notes, etc.)	$257,227,466[2]
Debt on which interest has ceased since maturity (payable on presentation)	1,459,630
Interest bearing debt (as a result of loans issued under various acts)	1,023,357,250
GROSS DEBT	$1,282,044,346
Balance available to pay maturing obligations	74,216,460
NET DEBT	$1,207,827,886

The annual interest charge on the interest bearing debt was $23,084,635 for the year ending June 30, 1916.

2. United Kingdom

Consisting predominately of the heritage of past wars, the aggregate gross liabilities of the United Kingdom of Great Britain and Ireland were composed of the following items on March 31, 1914:

National Debt, March 31, 1914[3]

Funded Debt	£586,717,872
Terminable Annuities	29,552,219
Unfunded Debt[4]	35,000,000
Total Dead Weight Debt	£651,270,091
Other Capital Liabilities	56,384,019
AGGREGATE GROSS LIABILITIES	£707,654,110

1 Financial Statement of the United States Government, March 31, 1917.

2 After deducting gold reserve of $152,979,025.

3 Parliamentary Paper No. Cd. 7426.

4 Including treasury bills temporarily paid off out of the exchequer balances. For purposes of comparison they must be included in the liabilities existing at the end of the year.

To meet the unforeseen expenditure resulting from the outbreak of the war in August, the government resorted to the issue of treasury bills. The situation called for a war budget and on November 17, 1914, Mr. Lloyd George presented the appended statement of the revised estimates for the year:

Estimates 1914-1915, presented November, 1914[1]

Estimated expenditure on peace basis		£206,924,000
Estimated war expenditure		328,443,000
Total 1914-1915		£535,367,000
Estimated revenue on existing basis		195,796,000
To be provided		£339,571,000
Additional resources:		
By new taxation	£15,500,000	
By suspension of the new sinking fund	2,750,000	
		18,250,000
Impending deficit		£321,321,000

The Chancellor announced that the deficit would be met by borrowing. By renewing the treasury bills expiring during the year, the amount to be raised by additional loans would be reduced to £230,321,000. However, the Chancellor considered it advisable to raise sufficient funds to finance the government through the following June, so the first war loan was fixed at £350,000,000.

This loan provided for an issue of £350,000,000 of war stock or bonds at 95, bearing interest at 3½%. It was to be repaid at par on March 1, 1928, with the possibility of repayment at any time on or after March 1, 1925, at the option of the government.[2] An undue strain upon the money market was avoided by spreading the payment of subscriptions over a period of five months ending April 26, 1915, with two ten per cent installments each month. As an added feature, the Bank of England agreed that

1 Debates, House of Commons, Vol. 68, col. 350.
2 Prospectus of the War Loan, November 17, 1914.

until March 1, 1918 it would advance against the deposit of war stock or bonds, amounts equal to the issue price, at a rate of interest one per cent below the current bank rate.[1] The loan was oversubscribed.

The condition of the debt at the close of the financial year is indicated below:

National Debt, March 31, 1915[2]

	Amount	Increase or decrease during 1914-1915
Funded Debt	£583,290,097	-£3,427,775
Terminable Annuities	28,040,721	-1,511,498
Unfunded Debt[3]	497,486,258	+462,486,258
Other Capital Liabilities	56,984,626	+600,607
AGGREGATE GROSS LIABILITIES	£1,165,801,702	+£458,147,592

The notable increase which had taken place in the unfunded debt as a result of the War Loan Act of 1914 was the outstanding feature among the debt transactions of the year.

Under this act there had been created:		
By issue of War Stock and Bonds	£350,000,000	
By issue of Exchequer Bonds	50,000,000	
By issue of Treasury Bills (net)	66,500,000	
		£466,500,000
But there had been redeemed during the year:		
War Stock and Bonds	£909,242	
Exchequer Bonds issued under various acts	3,104,500	
		4,013,742
Net increase in the Unfunded Debt		£462,486,258

In budgeting for another year of war, Mr. Lloyd George presented the following statement:

[1] Debates, House of Commons, Vol. 68, col. 374.
[2] Parl. Paper No. Cd. 7994.
[3] Including treasury bills temporarily paid off.

Estimates for 1915-1916[1]

Total estimated expenditure		£1,136,434,000
Revenue on existing basis of taxation	£267,232,000	
By suspension of the new sinking fund	3,780,000	
By additional taxation	3,100,000	
		274,112,000
Impending deficit		£862,322,000

In the latter part of June, 1915 Mr. McKenna pointed out that the realized deficit up to March 31, 1915 had totaled £334,000,000.[2] From March 31 until June 19, 1915 there had been a further deficit of £184,000,000, making a total of £518,000,000 which had been met by receipts other than revenue. The first war loan had provided £331,000,000; exchequer bonds, £48,000,000; and treasury bills £235,000,000, making £614,000,000 in all. Exchequer bonds paid off reduced this total to £597,448,000 of which about £80,000,000 was on hand. However, as a result of the assumption of liabilities of the Bank of England and the rapid increase in expenditure, a new loan was necessary.

It did not seem desirable to use treasury bills for this purpose; so the second war loan consisted of an offer of an unspecified amount of 4½% stock and bonds at par.[3] The loan was to terminate definitely on December 1, 1945, with earlier redemption at the option of the Government on or after December 1, 1925. Provision was made for bonds in denominations ranging as low as £5 to £25 to be issued through the Post Office, and 5s. vouchers were also arranged for. In the event of future war loan issues, stock and bonds of this issue were to be accepted at par plus accrued interest as the equivalent of cash for purposes of subscription for such issues. For the benefit of holders of other government stocks desiring to subscribe

1 Debates, Commons, Vol. 71, col. 1009.
2 Debates, Commons, Vol. 72, col. 951.
3 Prospectus, June 21, 1915.

to the new loan, a series of options was offered. Advantage of this opportunity of converting other forms of government debt into the new loan was taken to the extent indicated below, according to an announcement of the Chancellor.[1]

	Amount for Conversion	Amount existing prior to conversion
Consols....................	£204,000,000	£536,101,161
2½% Annuities...........	7,500,000	29,812,405
2¾% Annuities...........	1,000,000	3,813,566
3½% War Loan...........	135,000,000	350,000,000

In the Fall, a five-year Anglo-French external loan of $500,000,000, dated October 15, 1915, and bearing interest at 5% was placed in the United States.

When the final balance sheet for 1915-1916 was presented it showed an expenditure of £1,559,000,000 and a revenue of £337,000,000. The deficit had been met by borrowing approximately six hundred million pounds by the second war loan, one hundred and fifty-four million pounds by the sale of exchequer bonds, fifty million pounds by the Anglo-French loan and the balance by treasury bills.[2] The results of these various transactions as they affected the debt are given below.[3]

National Debt, March 31, 1916

	Amount	Increase or decrease during 1915-1916
Funded Debt..........	£318,460,277	-£264,829,820
Terminable Annuities..	26,158,871	-1,881,850
Unfunded Debt........	1,796,129,496	+1,298,643,238
Other Capital Liabilities	56,690,601	-294,025
	£2,197,439,245	+£1,031,637,543

The enormous increase in the unfunded debt had occurred in the following manner:

1 The Economist (London), July-Dec., 1915, p. 853.
2 Debates, Commons, Vol. 81, col. 1051.
3 Parl. Paper No. Cd. 8334.

Unfunded Debt Increased 1915-1916

Under the War Loan Act, 1915:		
By issue $4\frac{1}{2}\%$ Stock and Bonds	£900,831,583	
By issue 5% Exchequer Bonds	155,371,195	
By issue Treasury Bills (net)	493,427,000	
By issue War Saving Certificates	1,387,191	
By issue Other Debt	9,246,575	
Under the American Loan Act, 1915	51,369,863	
Ways and Means Advances (net)	19,896,500	
		£1,631,529,907

Unfunded Debt Reduced 1915-1916

$3\frac{1}{2}\%$ War Stock and Bonds	£286,316,358	
$4\frac{1}{2}\%$ War Stock and Bonds	834,511	
Exchequer Bonds	45,735,800	
		332,886,669
Net Increase in Unfunded Debt 1915-1916		£1,298,643,238

Mr. McKenna's estimates for 1916-1917 called for:

Total expenditure	£1,825,000,000[1]
Revenue	502,000,000
To be met by borrowing	£1,323,000,000

Heavy issues of treasury bills were made through the year, the amount outstanding in September 1916 being over a billion pounds. Other forms of loans were resorted to also. In August, a two-year American collateral loan of £50,000,000, dated September 1, 1916, was announced at 5%. It was followed by another American loan of £60,000,000, for three and five years, dated November 1, 1916 and bearing interest at $5\frac{1}{2}\%$. In December a loan

[1] Actual expenditure April 1, 1916 to March 31, 1917, £2,198,112,710. Actual revenue April 1, 1916 to March 31, 1917, £573,427,582.

of £10,000,000 at 6% was placed in Japan in the form of three-year exchequer bonds.

By the thirtieth of December, 1916, the national debt, including about £760,000,000 loaned to allies and dominions, was approximately £3,461,852,000.[1] It was not destined to remain at that figure long for in January, 1917, the prospectus of the third great war loan appeared. This offered two propositions to the public. One consisted of a five per cent loan, redeemable 1929-1947, issued at 95. The other was a 4 per cent loan, redeemable 1929-1942, issued at par with interest tax free. The amount of these loans was not specified. Provision was made for a sinking fund of $\frac{1}{8}$ of 1% a month of the amount of each loan. This fund was to be used for purchasing stock or bonds of either loan for cancellation when the market price fell below the price of issue. Whenever the unexpended balance of this sinking fund was £10,000,000, further accumulation was to cease for the time being.

According to an announcement by Mr. Bonar Law, the subscriptions to the third war loan were as follows:

Amount Subscribed to 1917 War Loan[2]

Applications through the Bank of England	£819,586,000
Treasury Bills converted	130,711,950
Applications through the Post Office.....	30,715,000
War Saving Certificates purchased.......	19,300,000
	£1,000,312,950

Of the amount applied for only £22,000,000 was subscribed to the tax free loan.

Before the close of the financial year 1916-1917 another collateral loan, consisting of one and two-year notes dated February 1, 1917 and amounting to $250,000,000 and bearing interest at 5½% was issued in the United States.

1 On May 2, 1917, in introducing the fourth war budget Mr. Bonar Law said that since the beginning of the war $4,110,000,000 had been advanced to Great Britain's allies and $710,000,000 to her dominions.

2 The Economist (London), March 3, 1917, p. 424.

War Borrowings of the British Government[1]
August 1, 1914—March 3, 1917

4% and 5% War Loan of 1917	£605,560,000
War Savings 5-Yr. Certificates	67,300,000
"Other Debt"	137,400,000
Treasury Bills	630,760,000
War Expenditure 2-Yr. Certificates	26,879,000
Ways and Means Advances	125,046,000
3½% War Loan, 1925-1928	331,798,000
3% Exchequer Bonds, 1920	31,547,000
4½% War Loan, 1925-1945	582,630,000
5% U. S. A. Loan (October 1915)	50,820,000
5% U. S. A. Coll. Loan (September 1916)	50,000,000
5½% U. S. A. Coll. Loan (October 1916)	60,000,000
5% Exchequer Bonds:	
Due October 1919	34,263,000
Due December 1920	237,829,000
Due October 1921	62,496,000
6% Exchequer Bonds	160,952,000
	£3,195,280,000

3. Loans of Other Belligerent Nations

The tables given below of the loans of other belligerent nations from the beginning of the war to the end of December 1916 are taken from the Journal of Commerce[2] and are supplemented by available information on loans since that time. Unless otherwise indicated these tables are in terms of dollars:

a. Canada

British government loan to Canada	$200,000,000
Ten-Year 4½% in London	25,000,000
One and Two-Year 5% in U. S.	45,000,000
Five, Ten and Fifteen-Year 5% in U. S. (April, 1916)	75,000,000
Internal Ten-Year 5½% (November 1915)	100,000,000
Internal Fifteen-Year 5% (September 1916)	100,000,000
Provincial and municipal	120,500,000
	$665,500,000

[1] The Statist, March 10, 1917, p. 397. This table does not appear to include the $250,000,000 Anglo-American Loan of February, 1917.
[2] January 2, 1917.

A new $150,000,000 twenty-year loan, dated March 1, 1917 has been heavily oversubscribed. It is a 5% loan, issued at 96. The use of war saving certificates has been instituted in Canada, and by the middle of March 1917 $4,099,565 three-year certificates had been sold.

b. India

Government internal 4%	$15,000,000
Treasury bills in London	17,500,000
	$32,500,000

A new five per cent Indian loan of £100,000,000 with maturity 1929-1947 has been announced in London recently.

c. Australia

5's in London	$10,000,000
Internal loan	50,000,000
Second internal loan	250,000,000
	$310,000,000

A 4½% loan of $90,000,000 offered in January 1917 was oversubscribed. A loan of £3,500,000 at 5½% has been reported since that time, and South Australia has issued a small loan to meet bonds maturing this year.

d. France

National Loan, 5%, November 1915	$3,100,000,000
National Loan, 5%, October 1916	2,275,000,000
National Defence Bonds, estimated	2,800,000,000
National Defence Obligations "	400,000,000
Advances from Bank of France	2,000,000,000
Advances from Bank of France to foreign governments	250,000,000
Bonds and notes in London	500,000,000
Advances from Bank of Algiers	20,000,000
Loans in U. S.	695,000,000
	$12,040,000,000

France placed a collateral loan in America, dated April 1, 1917 and amounting to $100,000,000. It is a

two-year loan at 5½%. In March, arrangements were pending for an issue of a French loan in Tokio to pay for war munitions. The amount was $13,000,000 at 6%.

e. Russia

War Loan, 5%, October 1914	$257,500,000
War Loan, 5%, February 1915	257,500,000
Exchequer Bonds, 4%, March 1915	310,000,000
Currency Loan, April 1915	105,000,000
War Loan, 5½%, May 1915	515,000,000
War Loan, 5½%, November 1915	515,000,000
War Loan, 5½%, April 1916	1,040,000,000
War Loan, 5½%, November 1916, estimated	1,000,000,000
Treasury Bills, 5%, estimated	2,000,000,000
Issues discounted in England	700,000,000
Issues in France	150,000,000
Loan in Japan	25,000,000
Three-Year 6½% credit in U. S.	50,000,000
Loan in U. S., 6%	50,000,000
Acceptances in U. S. (since paid)	25,000,000
Credit to Russian Asiatic Bank in U. S.	25,000,000
Treasury Notes, in U. S. 5%, One-Year (since paid)	10,000,000
	$7,035,000,000

Since January 1, 1917, Russia has renewed treasury bills expiring and has announced another great war loan. The amount offered was not limited and the probable amount subscribed has been placed at $1,500,000,000. The loan will pay 5% interest and is tax exempt.

f. Italy

National Loan, 4½%, December 1914	$200,000,000
War Loan, 4½%, July 1915	200,000,000
Twenty-five-Year 5's, approximate	1,200,000,000
Treasury Coupon Bonds, 5%	250,000,000
English Credit for War Supplies	250,000,000
One-Year 6% Notes in U. S.	25,000,000
	$2,125,000,000

Since the first of January, Italy has offered an unlimited 5% perpetual loan at 90. It is tax free and inconvertible prior to 1931. Subscriptions have exceeded 3,600,000,000 lire. (1 lire=$0.19295 at fixed rate of exchange).

g. Germany

Imperial Loan, 5%, September 1914	$1,120,000,000
Imperial Loan, 5%, March 1915	2,265,000,000
Imperial Loan, 5%, September 1915	3,040,000,000
Imperial Loan, 5%, March 1916	2,678,000,000
Imperial Loan, 5%, September 1916	2,675,000,000
Securities in U. S., estimated	25,000,000
Bank Loan in Sweden	10,000,000
Notes in U. S., 5%, nine months, paid	10,000,000
Notes in U. S., 6% basis, due April 1917	10,000,000
	$11,833,000,000

The treasury bills expiring in April have been renewed and another great war loan has been announced. The latter is in the form of an imperial 5% loan at 98, irredeemable before 1924, and exchequer bonds with interest at 4½% at the same price. The bonds are redeemable by drawings from January 1, 1918 at 110 per cent. The total of the new war loan has been unofficially reported as $3,103,110,000.

h. Austria-Hungary

Austrian Loan, 5½%, November 1914	$445,000,000
Austrian Loan, 5½%, June 1915	560,000,000
Austrian Loan, 5½%, November 1915	815,000,000
Austrian Loan, 5½%, May 1916	565,000,000
Austrian Loan, 5½%, Dec. 1916, estimated	500,000,000
Hungarian Loan, 6%, November 1914	244,000,000
Hungarian Loan, 6%, June 1915	223,000,000
Hungarian Loan, 6%, November 1915	240,000,000
Hungarian Loan, 6%, Dec. 1916, estimated	250,000,000
Loan from German bankers	113,000,000
Second loan in Germany	125,000,000
Credit in Germany	60,000,000
	$4,140,000,000

According to an official announcement the new money in the fifth Austro-Hungarian loan, December 1916, was 4,464,610,000 kronen which is considerably higher than the total estimate of $750,000,000 given above (1 krone = $0.20263 at fixed rate of exchange). A sixth Austrian war loan is expected shortly.

A complete statement of the public debt of the belligerent nations resulting from war financing is impossible at this time. The best available tabulation of public debts now obtainable has been furnished informally by the Bureau of Foreign and Domestic Commerce. It has not previously been published.

The Public Debts and Annual Debt Charges of European Belligerent Countries[1]

[*Compiled by the Research Division of the Bureau of Foreign and Domestic Commerce, Department of Commerce*]

	Officially Reported		Estimated Jan. 1, 1917	Debt Charge
	Date	Amount		
United Kingdom[2]	Mar. 31, 1916	$10,694,000,000	$16,847,000,000	$619,000,000
France	Jan. 1, 1914	6,348,000,000	16,035,000,000	580,000,000
Russia	Jan. 1, 1916	8,649,000,000	12,127,000,000	371,000,000
Italy	Dec. 31, 1916	4,718,000,000	4,718,000,000	191,000,000
Austria-Hungary	Aug. 1, 1914	4,123,000,000	8,263,000,000	352,000,000
Germany	Sept. 30, 1916	12,158,000,000	13,382,000,000	849,000,000
Total		$46,690,000,000	$71,372,000,000	$2,962,000,000

United Kingdom. The net borrowing of the British Government from beginning of the war to January 1, 1917 has totaled $13,789,707,000. The estimate of debt on January 1, 1917 is based on data published in the Economiste Europeén of February 9, 1917. The figure of debt includes about 3,700 million dollars advanced to Allies and British dominions. The amount of debt charges represents the official estimate for the fiscal year ending March 31, 1917. Actual payments appear to be somewhat higher.

France. The net increase in the public debt from the beginning of the war to August 31, 1916 has been officially reported as $7,757,153,000. The figure of debt charges represents payments made in 1916. For the first half of 1917 an appropriation of 415 million dollars has been asked by the Ministry of Finance.

[1] The debt of Canada was $328,485,000 July 31, 1914 and $867,771,000 December 31, 1916. *Journal of Commerce*, January 31, 1917.

[2] Mr. Bonar Law stated May 2, 1917 that the national debt was $19,270,000,000, less advances to the allies and dominions.

Russia. The amount of debt charges represents the budget estimate or 1917

Italy. The amount of debt charges represents the sum actually paid in 1916. The figures are from the Gazzetta Ufficiale.

Germany. The figures of debt relate to the Empire only, the debt of the various States not being included. As some of the war charges are borne by the States the figures do not include the total war debt. The debt service as shown, including interest, amortization, management and other charges, represents the budget estimates for the fiscal year ending March 31, 1918.

Austria-Hungary. The estimate of the debt does not include uncovered paper money in circulation. The amount of the latter has been estimated unofficially at about 2,500 million dollars.

TAXATION

Introductory

Before proceeding to describe in detail the tax measures introduced as a result of the war, it might be well to glance at the tax situation before the opening of hostilities, in order to understand the possibilities that suggested themselves to the legislators at a time when greater elasticity in revenue was sorely needed. The following table summarizes the yield of the various taxes, arranged under the four general heads, in 1912:[1]

Revenue of France, Germany and England from Taxation in 1912. (In millions of dollars).

Source	France		Germany		England	
	Revenue	Percentage of Total Revenue	Revenue	Percentage of Total Revenue	Revenue	Percentage of Total Revenue
1. Taxes on Wealth[2]	360	47%	290	43%	417	54%
2. Protective Duties[3]	76	9.9%	104	15.4%	3	0.4%
3. Taxes on Harmful Consumption and Pure Luxuries[3]	175	22.6%	89	13.2%	197	25.1%
4. Taxes on Necessary Consumption[3]	156	20.5%	192	28.4%	159	20.5%
Total	767	100.0%	675	100.0%	776	100.0%

[1] Pierre Leroy-Beaulieu, *Les Impôts et les Revenus en France, en Angleterre et en Allemagne*, Paris 1914, pp. 55-58.

[2] In this category are included taxes on incomes, successions and transfers, registration duties and stamp taxes.

[3] Many of the items which would ordinarily fall in the category of customs duties are distributed among the two following divisions according as they are taxes on harmful consumption and pure luxuries or taxes on useful consumption. The actual revenue from customs duties in 1912 was 168 million dollars in England, 164 million dollars in Germany and 132 million dollars in France.

It is evident that England has relied considerably more on taxes levied on wealth, than either France or Germany. Taxes on necessary or useful consumption yielded a greater revenue in Germany than elsewhere whereas taxes on harmful consumption and pure luxuries played a less important rôle in the fiscal realm of Germany than of France or England. Germany derived a greater proportion of its revenue from protective duties than France.

I. United States

The receipts and expenditures of the United States for the last four fiscal years have been as follows:

Receipts and Expenditures of the United States

	1913	1914	1915	1916
A. Receipts				
Customs..........	$318,891,395.86	$292,320,014.51	$209,786,672.21	$213,185,845.63
Internal Revenue.				
Ordinary........	309,410,665.81	308,659,732.56	283,398,760.85	303,486,474.04
Emergency (October, 22, 1914)..	....	....	52,069,126.29	84,278,302.13
Corporation Income Tax......	35,006,299.84	43,127,739.89	39,155,596.77	56,993,657.98
Individual Income Tax......	....	28,253,534.85	41,046,162.09	67,943,594.63
Sales of Public Lands..........	2,910,204.69	2,571,774.77	2,167,136.47	1,887,661.80
Miscellaneous....	57,892,663.64	59,740,370.13	70,287,372.90	51,889,016.28
Total Ordinary Revenue......	724,111,229.84	734,673,166.71	697,910,827.58	779,664,552.49
Public Debt Receipts..........	23,400,850.00	23,021,222.50	22,486,955.00	58,452,402.50
Postal Revenues..	266,619,525.65	287,934,565.67	287,248,165.27	312,057,688.83
Total Receipts...	1,014,131,605.49	1,045,628,954.88	1,006,349,780.54	1,153,044,639.10
B. Expenditures including postal...	1,010,812,448.78	1,045,600,861.09	1,063,792,290.29	1,072,894,093.23
Surplus...........	3,319,156.71	28,093.79	*57,442,509.75 *Deficit	80,150,545.87

With the opening of the Great European struggle in 1914, the treasury of the United States was seriously affected and Congress adopted the Emergency Revenue Act in October, imposing an elaborate system of stamp duties to meet the impending deficit of the year. This

Act was subsequently repealed and was later superseded by other measures which were intended to yield considerably more revenue with less administrative difficulty. The following is a detailed account of the war tax legislation now in force:

A. Income Tax. The rates were raised in the following manner: 2% on incomes exceeding $3000, if the recipient is single, and $4000, if married, but not exceeding $20,000; on incomes above $20,000 to $40,000, 1% super-tax; $60,000-$80,000, 3%; $80,000-$100,000, 4%; $100,000-$150,000, 5%; $150,000-$200,000, 6%; $200,000-$250,000, 7%; $250,000-$300,000, 8%; $300,000-$500,000, 9%; $500,000-$1,000,000, 10%; $1,000,000-$1,500,000, 11%; $1,500,000-$2,000,000, 12%; and on incomes above $2,000,000, 13%.

B. Estate Tax. The sum of $50,000 is exempt in every case. The rates are: 1.5% on taxable inheritances of $50,000 or less; 3% on sums ranging between $50,000 and $150,000; 4.5% on $150,000-$250,000; 6% on $250,000-$450,000; 7.5% on $450,000-$1,000,000; 9% on $1,000,000-$2,000,000; 10.5% on $2,000,000-$3,000,000; 12% on $3,000,000-$4,000,000; 13.5% on $4,000,000-$5,000,000 and 15% on amounts in excess of five millions.

C. Munition Manufacturers' Tax. A tax of 12.5% is levied on the net profits derived from the manufacture of gunpowder, cartridges, projectiles, firearms, electric motor boats, etc.

D. Capital Stock Tax. A tax is imposed amounting to 50c. for every $1000 of the face value of the capital stock of any enterprise, including the surplus and undivided profits. The sum of $99,000 is exempt.

E. Licenses.

Brokers	$30
Pawnbrokers	$50
Ship brokers	$20
Custom House brokers	$10
Theatres, Museums and Concert Halls	
Seating capacity of 250 or less	$25
Seating capacity 250-500	$50
Seating capacity 500-800	$75
Seating capacity above 800	$100
Proprietors of Circuses	$100
Proprietors of Bowling Alleys and Billiard Rooms	$5 for each alley or table
Manufacturers of Tobacco	
If annual sale does not exceed 50,000 lbs.	$3
If 50,000-100,000 lbs	$6
If 100,000-200,000 lbs	$12
If above 200,000 lbs	8c. per 1000 lbs.
Manufacturers of Cigars	
If annual sale is 50,000 cigars or less	$2
If 50,000-100,000	$3
If 100,000-200,000	$6
If 200,000-400,000	$12
If above 400,000	5c. per M.
Manufacturers of Cigarettes	3c. per 10,000

F. Excess Profits Tax. Every corporation or partnership must pay a tax of 8% on the amount by which its net income from all sources exceeds (a) $5000 and (b) 8% of the capital invested and employed in the business.

The capital invested embraces the actual cash paid in, the actual cash value of other assets at the time of paying the tax and the paid in or earned surplus and undivided profits.

G. Internal Revenue Charges.

Beer		$1.50 per bbl. of 31 gals.
Wine	If it contains 14% of absolute alcohol or less	4c. per gal.
	If it contains 14% to 21%	10c. " "
	If it contains 21% to 24%	25c. " "
	If it contains more than 24%, it is taxed as distilled spirits.	
Sparkling Wines, etc. (additional stamp tax)		
Champagne		3c. each half-pint
Carbonated Wine		1½c. " " "

II. Great Britain

Immediately upon the entrance of Great Britain into the European conflict, the Chancellor of the Exchequer clearly enunciated the policy of defraying a considerable part of the expenditures for war purposes by means of taxation.[1] The rates of the income tax for the remainder of the year 1914 were doubled, and were again raised in 1915 and in 1916. The customs and excise duties were altered so as to yield a greater revenue than heretofore. In 1915-1916, a new tax was imposed on excess profits arising as a result of the war. The latter source has proved to be extremely lucrative, even beyond the most liberal expectations of the Chancellor.

Although Great Britain has been unable to emulate its feats of the Napoleonic Wars when forty per cent of its expenditures is said to have been met by taxation, its present efforts that are directed along the same lines are none the less noteworthy, as they are singular. It is deriving an income from taxation that exceeds by all odds the tax revenue of any other belligerent country. The following table shows the tax and non-tax revenue of Great Britain during the War as compared with the normal year 1913-1914:[2]

[1] Cf. Lloyd George's Budget Speech, *Parliamentary Debates (Commons)*, N. S. Vol. 68, columns 348 *et seq.*

[2] These figures are taken from *Finance Accounts of the United Kingdom*, 1913-1914, 1914-1915, and 1915-1916. The statistics for parts of a fiscal year were secured from the *Economist* (London), April 7, 1917, p. 618.

Revenue of Great Britain Before and During the War

SOURCES	1913-1914	Aug. 1, 1914, to Mar. 31, 1915	1915-1916	1916-1917
1. Taxation:				
Customs........	£35,568,580	£27,613,492	£59,575,610	£70,561,000
Excise..........	39,657,957	30,827,167	61,207,683	56,380,000
Estate, etc. Duties	27,165,122	18,170,570	30,937,982	31,232,000
Stamps.........	9,983,363	4,375,792	6,779,998	7,878,000
Land Tax.......	690,006	2,288,067	2,654,865	2,580,000
House Duty	1,944,400			
Income Tax.....	47,240,770	62,508,854	129,160,589	205,033,000
Excess Profits...	....	....	187,846	139,920,000
Land Value Duty	734,892	363,961	368,816	....
Total..........	162,985,090	151,411,191	290,873,389	513,584,000
2. Non-Tax:				
Revenue [1]......	35,338,354	20,347,553	46,465,608	59,843,582
Grand Total...	198,323,444	171,758,744	337,338,997	573,427,582

The excise duties have not responded as well as might be expected but this is due to the fact that the tax, added to the high prices that already existed, discouraged consumption. The estate, stamps, house and land value duties have either remained stationary in yield or have declined. The revenue from the income tax, on the other hand, has more than quadrupled since 1913-1914. The receipts from the income tax in 1916-1917 alone exceed the total tax revenue during the normal year 1913-1914, and combined with the excess profits duty, it is greater than the total income from taxation during 1915-1916. The non-tax revenue has almost doubled since the fiscal year 1914.

The income tax and the excess profits duty afforded the greater part of the absolute increase in the total receipts during 1916-1917. In 1913, the total receipts were £198,323,444 and in 1916-1917 (up to March 17, 1917) they were £573,427,582—an increase of £375,104,138. To this increase, the income tax contributed £157,792,230 or 42% of the sum, and the excess profits duty £139,920,000 or 37.3%—together 79.3% of the total increase in revenue since 1913-1914.

When the expenditure side of the accounts is examined, it is found that owing to the war, this item has in-

[1] This item embraces post-office (telegraph and telephone included), crown lands, Suez Canal shares, and miscellaneous.

creased about twenty-one fold above normal in 1913. The table that is here given aims to show the total receipts from all sources and the expenditures for the respective years or parts of years:

Receipts and Expenditures of Great Britain [1]

YEAR	Total Receipts	Total Expenditures
1. 1913-1914	£198,242,897	£197,492,968
2. August 1, 1914-March 31, 1915	171,758,744	498,359,980
3. 1915-1916	336,766,824	1,559,158,377
4. 1916-1917	573,427,582	2,198,112,710
5. Grand Total August 1, 1914-March 31, 1917	1,081,953,388	4,255,631,067

The average daily expenditure for the period beginning with the opening of hostilities to the close of the fiscal year 1914 was £2,050,864; in 1915, it was £4,271,666, and in the fiscal year 1916 it rose to £6,022,226, or an increase of 193% above the daily average in 1914.[2]

In relating revenue to expenditure, interesting and highly instructive results are obtained. During the period between August 1, 1914 and March 31, 1915, the expenditures were, to recapitulate, £498,359,980 and the total revenue was £171,758,744 or 34.4% of the expenditures. In the fiscal year 1915, the expenditures were £1,559,158,377, and the revenue £336,766,824 or 21.6%. In spite of the increase in the revenue, the ratio dropped and this was in great part due to the marked rise in the expenditure side which was totally unforeseen at the time. In the year 1916, the expenditures were £2,198,112,710 and the revenue receipts were £573,427,582 or 26.0% of the former. For the whole period of the war, from August 1, 1914 to March 31, 1917, the expenditures were £4,255,631,067 and the receipts, £1,081,953,388 or 25.4% of the former. It is found, however, that in the expenditure accounts are included the loans to Allies and Dominions, which are estimated to amount to 964 million pounds up to March 31, 1917. Since these loans are issued by the

[1] *Finance Accounts,* and *Economist* (London) for April 7, 1917 *op. cit.*

[2] These figures already include expenditures to aid the Allies and Dominions.

British Government on its own credit and since they comprise a part of its national obligations, it is not wholly justifiable to omit this entire sum from the expenditure accounts, especially when the interest charges will have to be met in no small measure by Great Britain herself, as in the case of Belgium, Serbia and Montenegro. In some instances, it is highly doubtful whether these loans will ever be repaid. Assuming, however, that the contrary is true and that the estimate of 964 millions is correct, the revenue that has already flowed into the national coffers has defrayed 32.8% of the total net expenditure from the beginning of the war to March 31, 1917. The significance of this statement is manifest on the surface and requires no further comment.

A detailed analysis of the changes effected in the tax systems of Great Britain in effect May 1, 1917 follows. It will be noticed that while England has retained its free trade policy, the customs duties were as a rule considerably raised on those commodities that had already been subject to such imposts before the present conflict began.[1]

A. Income Tax: The general exemption was reduced to incomes below £130. Relief of £120 is granted if income does not exceed £400; £100, if between £400 and £500, and £100 if between £500 and £600. An additional relief of £25 is granted for each child, provided the income of the recipient does not exceed £700. The rates are as follows:

1. Earned incomes, 2s. 3d. per £ (11.25%), where the total earned and unearned income does not exceed £500;

2s. 6d.	(e. g. 12.5%)	where it is between	£500	and	£1000
3s.	(e. g. 15%)	" " " "	£1000	"	£1500
3s. 8d.	(e. g. 18.33%)	" " " "	£1500	"	£2000
4s. 4d.	(e. g. 21.66%)	" " " "	£2000	"	£2500
5s.	(e. g. 25%)	" " "	above £2500		

2. Unearned incomes, 3s. per £ where the total earned and unearned income does not exceed £300 (e. g. 15%);

3s. 6d.	(e. g. 17.5%)	where it is between	£300	and	£500
4s.	(e. g. 20%)	" " " "	£500	"	£1000
4s. 6d.	(e. g. 22.5%)	" " " "	£1000	"	£2000
5s.	(e. g. 25%)	" " "	above £2000		

An additional duty of 2s. per £ (e. g. 10%) is levied in respect to income from securities that are desired by the Chancellor, for credit purposes.

3. Super-tax: Where the total income exceeds £3000, the super-tax is levied: on the excess over £2500, the rate is 10d. per pound for the first £500 of excess (e. g. 4.16%).

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[1] Cf. 6 & 7 Geo. V, ch. 24; 6 Geo. V, ch. 11 and 5 & 6 Geo. V, ch. 89.

1s. 2d. per pound on sums between £3000 and £4000 (e. g. 5.83%)
1s. 6d. " " " " " £4000 " £5000 (e. g. 7.5%)
1s. 10d. " " " " " £5000 " £6000 (e. g. 9.16%)
2s. 2d. " " " " " £6000 " £7000 (e. g. 10.83%)
2s. 6d. " " " " " £7000 " £8000 (e. g. 12.5%)
2s. 10d. " " " " " £8000 " £9000 (e. g. 14.16%)
3s. 2d. " " " " " £9000 " £10,000 (e. g. 15.83%)
3s. 6d. " " " " " £10,000 " £11,000 (e. g. 17.5%)

Soldiers may claim a reduction of their income tax in respect to their pay as follows:

9d. per pound if the total income does not exceed £300 (e. g. 3.73%)
1s. 3d. " " " " " " is between £300 and £500 (e. g. 6.25%)
1s. 9d. " " " " " " " " £500 " £1000 (e. g. 8.25%)
2s. 3d. " " " " " " " " £1000 " £1500 (e. g. 11.25%)
2s. 9d. " " " " " " " " £1500 " £2000 (e. g. 13.75%)
3s. 3d. " " " " " " " " £2000 " £2500 (e. g. 16.25%)
3s. 6d. " " " " " " " above £2500 (e. g. 17.5%)

B. Excise and Customs Duties:

		Customs			Excise		
		£	s.	d.	£	s.	d.
1. Cocoa	cwt.	2	2	0			
husks and shells	cwt.		6	0			
butter	lb.		0	4½			
2. Coffee							
kiln dried, roasted or ground	cwt.	2	2	0			
otherwise	lb.	0	0	6			
substitute	lb.					0	1½
3. Chicory							
raw or kiln dried	cwt.	1	19	8	1	18	6
roasted or ground	lb.		0	6			
4. Sugar							
when tested by polariscope and found to have a polarization of 98°	cwt.	0	14	0	0	11	8
not exceeding...76°		0	6	9	0	5	7
Between 76° and 77°		0	6	11.3	0	5	9.4
" 77° " 78°		0	7	2.0	0	5	11.6
" 78° " 79°		0	7	4.7	0	6	1.9
" 79° " 80°		0	7	7.3	0	6	4.1
" 80° " 81°		0	7	10	0	6	6.4
" 81° " 82°		0	8	0.7	0	6	8.6
" 82° " 83°		0	8	3.4	0	6	10.8
" 83° " 84°		0	8	6.4	0	7	1.4
" 84° " 85°		0	8	9.5	0	7	3.9
" 85° " 86°		0	9	0.5	0	7	6.4
" 86° " 87°		0	9	3.5	0	7	8.9
" 87° " 88°		0	9	6.9	0	7	11.7
" 88° " 89°		0	9	10.2	0	8	2.5
" 89° " 90°		0	10	2.3	0	8	5.9
" 90° " 91°		0	10	6.3	0	8	9.2
" 91° " 92°		0	10	10.3	0	9	0.6
" 92° " 93°		0	11	2.4	0	9	4.0
" 93° " 94°		0	11	6.4	0	9	7.3
" 94° " 95°		0	11	10.4	0	9	10.7
" 95° " 96°		0	12	2.4	0	10	2
" 96° " 97°		0	12	6.5	0	10	5.4
" 97° " 98°		0	12	10.5	0	10	8.8

5. Molasses							
If containing 70% or more of sweetening matter	cwt.	0	8	10.5	0	7	4.5
70%-50%	"	0	6	4.5	0	5	3.5
50% or less	"	0	3	1.5	0	2	7.5
6. Glucose							
Solid	"	0	8	10.5	0	8	10.5
Liquid	"	0	6	4.5	0	6	4.5
7. Saccharine	oz.	0	4	6	0	4	6
8. Tea	lb.	0	1	0			

9. Other customs Duties:

Dried Fruits, Currants .... 2s. per cwt.
others .... 10s. 6d. per cwt.

Tobacco (a) Unmanufactured:
Containing 10 lbs. or more of moisture in every 100 lbs. weight thereof .... 5s. 6d. per lb.
Stripped .... 5s. 7d. " "
Containing less than 10 lbs .... 6s.1.5d. " "
Stripped .... 6s. 2d. " "

(b) Manufactured:
Cigars .... 10s. 6d. " "
Cavendish or Negro-head .... 8s. 6d. " "
Snuff containing more than 13 lbs. of moisture in every 100 lbs. weight .... 6s.7.5d. " "
Snuff containing less than 13 lbs .... 8s. " "
Cigarettes .... 8s. 6d. " "
Other manufactured tobacco .... 7s. " "

Wine .... Not exceeding 30° of proof spirit .... 1s. 3d. per gal.
Exceeding 30° but not above 42° .... 3s. " "
For every degree above 42° .... 3d. " "
Sparkling wine in addition .... 2s. 6d. " "
Still wine in bottle .... 1s. per gal. in addition

Beer .... Not exceeding 1215° .... £1 13s. for 36 gals.
Exceeding 1215° .... £1 18s. " " "
Others of 1055° specific gravity .... 8s. 3d. " " "

Gasoline .... 6d. per gal.

Spirits .... 18s. 10d. per proof gal.
If imported in bottle, enumerated, tested or sweetened .... 1s. per proof gal.
Liqueurs and cordials .... £1 6s. 6d. per gal.
Perfumed .... £1 10s. 1d. " "
Additional if imported in bottle .... 1s. " "

Chloroform .... 4s. 4d. per lb.

Chloral Hydrate .... 1s. 9d. per lb

Collodion .... £1 14s. 11d. per gal.

Ether .... Acetic .... 2s. 7d. per lb.
Butyric .... £1 1s. 10d. " gal.
Sulphuric .... £1 16s. 6d. " "

Ethyl .... Bromide .... 1s. 5d. per lb.
Chloride .... £1 1s. 10d. " gal.
Iodide .... 19s. " "

Playing Cards .... 3s. 6d. per pack

Matches....Customs	....	3s. 6d. per 10,000
Excise	....	3s. 4d. " 10,000
(If in boxes of more than 80 each, 1s. 9d. and 1s. 8d. respectively)		
Motor Cars, Motor Cycles and parts	....	33⅓% ad valorem
Clocks, Watches and parts	....	33⅓% ad valorem
Musical Instruments	....	33⅓% ad valorem
Cinema Films		
Negatives	....	8d. per linear ft.
Positives	....	1d. " " "
Blank	....	½d. " " "
Table Waters		
If prepared with sugar, etc	....	4d. per gal.
Otherwise	....	8d. " "

C. Excess Profits Duty: £200 exempt, 50% duty raised to 60%. The standard is the average profits during any two years of the three years preceding 1914. If no pre-war standard is possible, seven per cent of the capital employed is taken as the base in the case of individuals and six per cent in the case of corporations.

D. Entertainment Admissions:

Excise duty of ½d. where payment does not exceed 2d.
" " " 1d. if " is between 2d. and 6d.
" " " 2d. " " " " 6s. and 2s. 6d.
" " " 3d. " " " " 2s. 6d. and 5s.
" " " 6d. " " " " 5s. and 7s. 6d.
" " " 1s. " " " " 7s. 6d. and 12s. 6d.
" " " 1s. for every 10s. or fraction above 12s. 6d.

III. France

During the first year or two of the war, very few changes, if any, were made in the fiscal system of France, which were equal in magnitude to those introduced in Great Britain. It must be remembered that the occupation of French territory by the Germans early in the struggle made serious inroads on the national revenue, and were it not for the marked rise in the yield of customs duties occasioned by the expansion of foreign commerce, notably with the United States, this withdrawal of receipts might have produced disastrous results. The French legislators were slow in adjusting the revenue to the tremendous and unprecedented demands made upon the country as a result of the conflict and the fiscal situation was far from encouraging.

In 1916 and in the early part of the present year, alterations were made of far-reaching significance. An income tax law was introduced and passed in 1916, with a

proportional rate of 2% on amounts exceeding 5,000 francs, coupled with a system of abatements which rendered the tax progressive. However, the rates were changed later, as will be indicated in greater detail in the latter part of this section. An excess profits duty was levied, and a war tax was imposed upon those who were exempt from military service. Many of the taxes falling under the category "assimilated taxes" were doubled, the impost on the income from personalty was advanced considerably, new excise duties were imposed and the telephone, telegraph and postal charges were all revised to yield a larger income than hitherto.

A glance at the table here presented will indicate the revenue situation of France from 1913 through 1916. It is observed that the only sources that have responded to the increased needs occasioned by the war are the import duties and the tax on the income from personalty. All the other items have suffered a reduction during the war. In the non-tax revenue group, the income from public domain has displayed a tendency to increase beyond its normal yield.

Revenue of France 1913, 1914, 1915 and 1916.[1]

	1913	1914	1915	1916
	Francs	*Francs*	*Francs*	*Francs*
A. Tax Revenues:				
Direct Tax	562,815,768	574,429,449	548,929,516	492,015,839
Assimilated Taxes	59,518,262	61,501,987	64,877,570	48,703,402
Registration	833,667,000	615,011,000	463,594,500	524,617,000
Stamps	239,631,500	195,952,000	146,167,500	157,638,000
Bourse Operations	9,842,500	5,718,500	1,312,000	2,342,000
Income from Personalty	138,049,000	153,340,000	157,782,000	181,432,500
Import Duties	754,382,000	577,613,000	764,144,000	1,399,421,000
Indirect Taxes	673,928,000	562,108,000	477,069,000	472,902,000
Tax on Mineral Oil	1,983,000	1,455,000	227,000	462,000
Tax on Salt	35,239,000	33,717,000	31,854,000	30,954,000
Tax on Sugar	179,591,000	148,191,000	204,763,000	173,097,000
Total	3,488,647,030	2,929,036,936	2,860,720,086	3,483,584,741
B. Non-Tax Revenue:				
Monopolies	1,015,777,000	931,061,400	837,570,300	942,643,400
Domain, etc.	135,133,500	124,008,600	185,681,100	240,204,100
	1,150,910,500	1,055,070,000	1,023,251,400	1,182,847,500

[1] These figures are all taken from the *Journal Officiel de la République Française.* 1 franc = $0.19295 at fixed rate of exchange.

The monthly expenditure has grown from 1,340 million francs in 1914 to 3,191 million francs in 1917.[1] The following figures indicate the authorized expenditure up to June 30, 1917.

Five months of 1914	8,898,583,901	francs
Fiscal year 1915	22,804,486,525	"
Fiscal year 1916	32,635,943,250	"
First six months of 1917	18,570,959,650	"
Total	82,909,973,326	"

It has been estimated by the French Minister of Finance, M. Ribot, that the receipts from taxation will amount to 12,144,639,000 francs from August 1, 1914 to June 30, 1917. Assuming these figures to be approximately correct, it is found that the French people are meeting only 14.6% of the authorized expenditure out of taxation. The remainder of the bill is covered by advances from the Bank of France, loans, etc.

When a comparison is made between Great Britain and France with respect to the emphasis placed on direct taxation, an interesting conclusion stands forth. It is discovered that the former is now obtaining 73% of its resources from direct taxation as compared with 47% in 1913. France, on the other hand, is securing 39% of its present revenue from direct sources, as compared with 47% in 1913. Both France and England relied almost equally on direct taxation before the war, but since then a gap has appeared and the two countries are now proceeding to opposite extremes. The customs duties have doubled in France in the fiscal year 1916, which aided to swell the total of indirect taxes. In England the income tax has displayed a truly remarkable and almost incredible development, and combined with the enormous yield of the excess profits duty, it has very largely contributed to the prominence of direct taxation. The following table indicates the results in detail:

[1] *Annalist*, March 12, 1917, p. 367.

Direct and Indirect Taxation Compared in Great Britain and France.

A. FRANCE (Francs)

	1913	1914	1915	1916
Direct Taxes:				
Contribution Direct..........	562,815,768	574,429,449	548,929,156	492,015,839
Assimilated Taxes	59,518,262	61,501,987	64,877,570	48,703,402
Donations & Successions.......	357,010,000	248,899,500	243,828,500	263,860,000
Income from Personalty.......	138,049,000	153,340,000	157,782,000	181,432,500
Total Direct...	1,117,393,030	1,038,170,936	1,015,417,226	986,011,741
Indirect Taxes...	2,371,254,000	1,890,866,000	1,845,302,860	2,497,573,000
Direct Taxes as Percentage of Total..........	47.1%	54.9%	55.0%	39.4%
Indirect Taxes as Percentage of Total..........	52.9%	45.1%	45.0%	60.6%

B. GREAT BRITAIN (Pounds)

	1913	1914	1915	1916
Direct Taxes:				
Estate Duties....	27,165,122	28,542,570	30,937,982	31,232,000
Land and House Tax..........	2,684,406	2,548,067	2,654,865	2,580,000
Income Tax.....	47,240,770	69,544,854	129,160,589	205,033,000
Land Value Duty...	734,892	413,961	368,816	....
Excess Profits Duty.	....	....	....	139,920,000
Total Direct.	77,825,190	101,049,452	163,122,252	378,765,000
Indirect Taxes:				
Customs........	35,568,580	39,150,492	59,575,610	70,561,000
Excise..........	39,657,957	42,419,167	61,207,683	56,380,000
Stamps.........	9,983,363	7,434,792	6,779,998	7,878,000
Total Indirect..	85,209,900	89,004,451	127,563,291	134,819,000
Direct Taxes as Percentage of Total..........	47.7%	53.1%	56.1%	73.7%
Indirect Taxes as Percentage of Total..........	52.3%	46.9%	43.9%	26.3%

The recent changes that have been made in the French tax systems follow.

(a) Income Tax: [1] Sum of 3,000 francs is exempt. On 3,000-8,000 francs, the rate is 1%; 8,000-12,000 fr. 2%; 3% on 12,000-16,000 fr.; 4% on 16,000-20,000 fr.; 5% on 20,000-40,000 fr.; 6% on 40,000-60,000 fr.; 7% on 60,000-80,000 fr.; 8% on 80,000-100,000 fr.; 9% on 100,000-150,000 fr. and 10% on the surplus. Reduction of 5% of the principal of the tax is allowed when the recipient has one dependent; 10% if two; 20% if three and 10% for each additional one.

(b) War Tax: Tax of 12 francs and increase of 25% of income tax payable, levied on (1) those declared unfit or retired from service before August 1, 1914; (2) those in auxiliary service, etc.

(c) Grouped Taxes: The taxes on mining royalties, carriages, horses, mules, billiard tables, clubs, associations, meeting places and game keepers are all doubled. In the case of concessions not worked for ten years, the tax is raised to 5 fr. per hectare.

(d) War Profits: 60% of the profits realized by the war above 500,000 fr. as of January 1, 1916. Otherwise the old rate of 50% remains in force. The average profits during the three years prior to August 1914 are taken as the basis for measuring the extraordinary profits as a result of the war.

(e) Sale of Ships: A tax of 50 centimes per 100 francs is charged on the price of sale or charter of vessels of above 100 tons.

(f) Securities: Tax of 5% on income of securities and of 10% on prices paid in connection with state, municipal and other bonds. Tax of 6% on certain classes of foreign securities and foreign government loans. Fees due to directors are all taxed 5%.

(g) Theatres: Tax of 10 centimes on seats costing 1 fr. or less; 25 centimes on 1.05 fr.-8 fr. and 50 centimes on seats above 8 francs in value. Seats in state theatres are untaxed below 5 francs and in municipal theatres, 3 fr.

Music Halls: 20 centimes on seats up to 1½ fr.; 40c. on 1.55-4 fr.; 60c. on 4.05-8 fr. and 1 fr. if above 8 fr.

Cinematographs: Tax on gross monthly receipts of 5% up to 25,000 fr.; 10% on 25,000-50,000 fr.; 20% on 50,000-100,000 fr. and 25% on 100,000 fr. and above.

(h) Alcoholic Drinks:

50c. per hectolitre on right to manufacture beer
1½fr. " " " " " move cider, perry and mead
3fr. " " " " " " ordinary wine and 10 fr.

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[1] *Journal Officiel de la République Française*, December 31, 1916.

per 100 kilograms of dried grapes used in manufacturing wine for home consumption.

(i) Mineral Waters: (a) If the factory price is less than 20 centimes per bottle of ½ litre the tax is 1 centime; per bottle of more than ½ litre, 2 centimes;

(b) If the price is more than 20 centimes per bottle of ½ litre, the tax is 3 centimes; otherwise, 6 centimes. Preparations for the manufacture of mineral waters are taxed at 2 centimes on the amount needed to produce a litre of water.

(j) Pharmaceutical Products: A tax on retail selling price: 5c. on products selling at less than 50c.; 10c. on 50c. to 10 fr. and 50c. for every 5 fr. or fraction thereafter. Only those products are taxable to which a special name is given, or for which priority of invention is claimed or which are advertised without publication of the chemical formula. Ordinary drugs prepared and sold by chemists are excluded.

(k) Colonial Products:

Coffee and chicory root,	30 fr.	per 100 kilograms
Cocoa, husks or shells,	20 fr.	" " "
Chocolate with over 55% cocoa,	26 fr.	" " "
Chocolate with 55% cocoa or under,	14 fr.	" " "
Pepper, all-spice and imitations,	104 fr.	" " "
Amomum, cardamom, cinnamon,etc.	40 fr.	" " "
Nutmegs without husks, and mace	60 fr.	" " "
Vanilla	80 fr.	" " "
Tea	40 fr.	" " "
Sugar, refined and raw	40 fr	" " "
candies	42 fr. 80c.	" " "
molasses	2 fr.	" " "
glucoses	9 fr.	" " "
Tobacco, small packets to consumers	15 fr.	" " "
retail	14 fr.35c.	" " "

(l) Postal Taxes:

(a) postal rates advanced.

(b) telegraph messages: from 15c. on telegrams not exceeding 10 words to 50c. on above 50 words, etc. Additional tax on express letters, private lines, wires rented or conceded to the press, etc.

(c) telephone: (a) local calls 5 centimes.
(b) trunk calls, from 5c. on 25c. message to 50c. on 2 fr. message.

(d) money orders: 5 centimes on money orders up to 20 fr.
10 " " " " " " 20-500 fr.
20 " " " " above 500 fr.

IV. Other Countries

A. Germany. Germany's method of financing the war stands in contradistinction to that of Great Britain. The view that the enormous expenditures occasioned by war should be partly defrayed out of taxation has found no strong place among the fiscal policies of German statesmen. One explanation of this phenomenon is the lack of elasticity in the revenues of the Imperial Government. The central authorities had always reserved for themselves the field of indirect taxation; the individual states, on the other hand, had relied considerably and often mainly on direct taxation. Consequently, with the rise in the expenditures of the latter, the burden of taxation became much heavier than in peace times and it became impossible even to contemplate raising revenue for Imperial purposes by direct means.

Furthermore, it was the intention of the military authorities of the Central Powers, at the outbreak of the war, to attack France and crush her completely before Great Britain could mobilize its resources and come to the aid of France and then to proceed similarly in the case of Russia. By such a speedy and decisive victory, it was held that Germany could easily impose an indemnity to cover its sacrifices and so free its own people of any possible war burdens. As it happened, matters turned out differently, but the hope of an indemnity was never given up. Although at times it seemed to languish, the Imperial Minister of Finance, Dr. Karl Helfferich, made an open secret of this fact and continually referred to it as a foregone conclusion. From a glance at the present military situation, however, it seems that this illusion will have to be dispelled and that the German financiers will soon have to face the cold fact that Germany is now waging a war almost entirely on credit, to the detriment of future generations.

Data are completely lacking as to the actual receipts and expenditures from 1914 to 1917. No effort was spared to find these figures, but with little or no success. The

table here appended gives the receipts as contained in the Imperial budget for the years 1913, 1914 and 1915:

Revenues of Germany in 1913, 1914 and 1915[1] (in marks)

Source	1913	1914	1915
1. Post and Telegraph	833,314,600	881,286,500	881,569,500
2. Printing-office	15,742,800	13,885,000	13,885,000
3. Railroads	158,580,200	162,246,000	162,246,000
4. Various Administrative Receipts	91,565,600	81,961,000	79,822,700
5. Taxation:			
Customs	679,321,800	712,930,000	712,930,000
Tobacco	11,415,000	10,876,000	10,876,000
Cigarettes	42,699,300	39,202,000	39,202,000
Sugar	173,745,700	163,252,000	163,252,000
Salt	62,386,300	61,144,000	61,144,000
Spirits	193,774,700	193,995,000	193,995,000
Vinegar	799,100	825,000	825,000
Wine	9,511,300	9,970,000	9,970,000
Lamps and Bulbs	15,072,100	15,866,000	15,866,000
Matches	20,130,700	21,035,000	21,035,000
Beer	130,005,300	128,950,000	128,950,000
Cards	2,003,800	2,033,000	2,033,000
Stamp Tax on Bills	19,615,500	19,100,000	19,100,000
Stamps (general)	235,034,500	250,085,000	264,085,000
Increment Tax	15,322,900	100,000	100,000
Inheritance	46,356,800	50,000,000	50,000,000
Miscellaneous	2,084,700	1,919,000	1,919,000
6. Contributions for Defence	820,600	393,820,900	327,740,900
7. Contributions from the States	51,940,800	51,940,800	51,940,800
8. Miscellaneous	383,155,300	138,755,300	104,593,600
Total	3,194,399,400	3,405,178,400	3,323,081,400

B. Canada. Canada has recently added new war taxes to meet the expenditures arising as a result of her participation in the struggle of the Empire. The total receipts in 1916 were $172,147,838.27, distributed as follows:

Receipts of Canada, 1916[2]

Customs	$98,649,409.48
Excise	22,428,491.58
Post Office	18,858,690.10

[1] *Statistisches Jahrbuch für das Deutsche Reich*, 1915, pp. 347-348. The figures for 1914 and 1915 are budgetary estimates. Although the publication came out in 1915 when the receipts for 1914 could have already been ascertained, the actual revenue is not given, perhaps to conceal the true situation at the time.

[2] Canadian Year Book, 1917.

Revenue from Public Works.....	352,918.79
Revenue from Minor Public Works	58,868.50
Revenue from Railways.........	18,427,908.65
Revenue from Canals..........	446,722.21
Interest on Investments........	3,358,210.13
Patent Fees..................	230,191.95
Casual.......................	1,328,124.09
Dominion Lands...............	2,299,550.47
Inspection of Staples Revenue..	913,616.46
War Tax Revenue.............	3,620,781.72
Miscellaneous................	1,174,354.14

The expenditures for 1916 were $130,350,726.90, leaving a net surplus of $41,797,111.37.

Since 1881, the total debt of Canada has risen almost four-fold and the net debt three-fold. The following table indicates the debt and interest for various years:

Debt and Interest on Debt

	Total Debt	Net Debt	Interest Paid on Debt	Rate of Interest on Gross Debt
1881..........	$199,861,537.51	$155,395,780.40	$7,591,144.88	3.79
1885..........	264,703,607.43	196,407,692.14	9,419,482.19	3.55
1890..........	286,112,295.10	237,533,211.77	9,656,841.16	3.37
1895..........	318,048,754.87	253,074,927.09	10,466,294.44	3.29
1900..........	346,206,979.92	265,493,806.89	10,699,645.20	3.09
1905..........	377,678,579.80	266,224,166.63	10,630,115.05	2.81
1910..........	470,663,045.99	336,268,546.33	13,098,160.61	2.78
1913..........	483,232,555.24	314,301,625.68	12,605,882.48	2.61
1914..........	544,391,368.86	335,996,850.14	12,893,504.95	2.37
1915..........	700,473,814.37	449,376,083.21	15,736,742.94	2.24
1916..........	943,839,433.92	615,156,171.02	21,421,584.86	...

The following excise duties and war taxes are now in force:

A. Excise Duties.

Acetic Acid..............................4c. per gal.
Malt.....................................3c. per lb.
Imported...........................5c. per lb.
Malt Liquor..............................15c. per gal.
Spirits....When the material used in the manufacture consists of not less than 90% of unmalted grain or when manufactured from sugar, molasses, etc............$2.40 per proof gal.

When manufactured from malt barley exclusively .... $2.42 per proof gal.
When manufactured from molasses exclusively .... $2.43 per proof gal.
When used in manufacture of perfumery. 75c. per gal.
When used in manufacture of soaps ..... 15c. per gal.

Fusel Oils .... 15c. per standard gal.

Vinegar .... 4c. per gal.

Tobacco . .

Cigarettes
Not more than 3 lbs. per 1000 .... $3 per 1000
More than 3 lbs. per 1000 .... $8 per 1000
Cigars .... $3 per 1000
In pkgs. of less than 10 cigars .... $4 per 1000
Snuff .... 10c. per lb.
Smoking, Chewing, Plug Twist, etc...... 10c. per lb.
Common Canadian Twist made from tobacco grown in Canada .... 10c. per lb.
All Foreign Leaf, unstemmed .... 28c. per lb.
All Foreign Leaf, stemmed .... 42c. per lb.
All manufactures where less than 50% of Canadian raw tobacco is used and 10% or more of other material .... 16c. per lb.

Wines.... Grape (non-sparkling), 3c. per pint, 5c. per quart, etc.
Champagne and sparkling, 13c. per half pint, 25c. per pint.

B. War Taxes.

Bank Note Circulation, ¼ of 1% on average amounts in circulation during the last days of December, March, June and September.

Trust and Loan Companies, 1% on gross amount of interest from loans and investments in Canada and from other business.

Insurance Companies, 1% of net premiums after January 1, 1915 (life, marine and fraternal exempt).

Telegrams .... 1c. each

Railroad and Steamship Tickets

(a) 5c. on tickets costing $1 to $5 and 5c. for every $5 above or fraction thereof, if the destination is Canada, Newfoundland, West Indies, Bermudas, British Guiana, Honduras and the United States.

(b) Otherwise, the tax is $1, if ticket costs more than $10; $3, if above $40 and $5, if above $65.

Sleeping Cars, 5c. for each seat and 10c. for each berth.
Promissory Notes, Bills of Exchange, Checks, etc. . . 2c.
Letters, Post Cards .... 1c.
Perfumery and Patent Medicine, 1c. for every 25c. of purchase price.

War Profits, 25% of excess above 7% of the capital engaged, if corporation, and above 10% otherwise. ($50,000 business exempt; also life insurance companies and farming industry).

C. Russia. The abolition of the *vodka* monopoly soon after the opening of hostilities left Russia in a sad fiscal plight. In 1913, the receipts from this source were 899,299,000 roubles;[1] in 1914, 503,904,000 roubles, and ac-

[1] 1 rouble—$0.51456 at fixed rate of exchange.

cording to the revised estimates for 1915 and 1916, they were 114,260,000 and 49,860,000 roubles respectively, or a reduction of 94% in the revenue.

In the table of "Receipts of Russia" printed on this and the following pages the totals here cited with regard to *VODKA* receipts do not appear in detail as they are divided up under several heads in the government statement, such as "liquor," "spirit monopoly."

The following table shows clearly the financial situation, as judged from the revised estimates for 1916 and 1915 in comparison with the actual receipts in 1914 and 1913:

Receipts of Russia[1] (in roubles)

	Revised Estimate for		Actual Receipts	Actual Receipts
	1916	1915	1914	1913
A. Direct Taxes:				
Land, Real Estate and Personal	118,953,876	116,364,770	....	....
On Commerce and Industries	192,660,500	210,499,500	....	....
Interest Payable on Securities	48,060,000	47,701,000	....	....
Total	359,674,376	374,565,270	280,557,000	272,517,000
B. Indirect Taxes:				
Liquor	25,261,000	60,418,000	....	....
Tobacco	149,594,000	111,706,500	....	....
Excise on Cigarette Papers	8,063,000	10,854,000	....	....
Sugar	190,853,000	177,600,000	....	....
Petroleum	82,040,200	62,040,200	....	....
Matches	43,517,700	43,515,500	....	....
Customs	314,400,000	233,050,100	....	....
Total	813,728,900	699,184,300	708,101,000	661,453,000
C. Duties:				
Stamps	128,209,400	138,039,295	....	....
Transfers of Property	32,190,000	53,215,000	....	....
Harbor Dues	6,000,000	8,000,000	....	....
Transportation Duties (passengers and goods)	240,000,000	286,000,000	....	....
Fire Insurance	10,000,000	10,000,000	....	....
Miscellaneous	27,202,200	18,659,237	....	....
Total	443,601,600	513,913,532	209,105,000	231,230,000

[1] Russian Year Book, 1916, pp. 590, *et seq.*

Receipts of Russia (in roubles)—*Continued*

	Revised Estimate for 1916	Revised Estimate for 1915	Actual Receipts 1914	Actual Receipts 1913
D. Royalties				
Mines	398,000	374,000	....	....
Mint	34,637,800	16,758,050	....	....
Postal Revenue	94,680,000	109,050,000	....	....
Telegraph and Telephone	70,600,000	55,730,000	....	....
Spirit Monopoly	51,360,000	144,260,000	....	....
Total	251,675,800	326,172,050	646,901,000	1,024,883,000
E. Property and Funds Belonging to the State				
Rents	41,628,587	44,320,773	....	....
Forests	95,890,500	85,748,900	....	....
State Railways	728,682,000	848,578,650	....	....
State Works and Mills	25,641,429	25,824,814	....	....
Interest on Funds, etc	124,279,800	39,890,800	....	....
Share in Profits of R. R.	14,708,000	26,474,000	....	....
Total	1,030,830,316	1,070,837,937	964,520,000	1,043,741,000
F. Expropriation of State Property	1,273,869	1,826,790	1,074,000	2,857,000
G. Payments in Redemption of Land	1,563,586	1,864,863	1,931,000	1,194,000
H. Reimbursements of Treasury	112,552,414	128,697,152	107,502,000	116,677,000
I. Miscellaneous	17,248,457	15,112,420	25,055,000	16,160,000
Total Ordinary Revenue	3,032,149,318	3,132,174,314	2,898,098,000	3,417,360,000
Total Extraordinary "	614,435,259	70,318,878	....	....
Grand Total	3,646,584,577	3,202,493,192	2,898,098,000	3,417,360,000
Ordinary Expenditure	3,174,124,000	3,068,055,000	2,927,099,000	3,094,248,000

During 1915 and 1916 two important fiscal measures were introduced, *viz.*, an excess profits duty and a general income tax. The former went into effect January 1, 1916 and affected all companies and profit-making concerns. In addition to the ordinary industrial tax,[1] the excess profits duty is levied on all profits in excess of 8% of the capital employed in the business and in excess of the average profits in 1913 and 1914. This law applies to profit-

[1] The industrial tax ranges from 5% on profits exceeding 3% of the capital employed to 11½% on profits amounting to 20% of the capital. Salaries of members of the Board, general managers, their assistants and attorneys are taxed 1%, if between 3000 and 5000 roubles; 2%, if 5000-10,000; 4%, if 10,000-15,000; 5%, if 15,000-20,000 and 6%, if above 20,000 roubles.

making concerns that are not subject to the ordinary industrial tax (provided the excess is 500 roubles) and to the salaries and remunerations of directors, members of the council of the committee of auditors, managers, assistant managers and attorneys of limited liability companies, (provided the increase above 1913 and 1914 is in 500 roubles or more). For the latter category, the rate is 20% on the increase. In all other cases, the rates are progressive in the following manner:

If the profits on the capital are between	8%	and	9%,	the tax is	20%	of the inc.
" " " " " " " "	9%	"	10%,	" " "	21%	" " "
" " " " " " " "	10%	"	11%,	" " "	22%	" " "
" " " " " " " "	11%	"	12%,	" " "	23%	" " "
" " " " " " " "	12%	"	13%,	" " "	24%	" " "
" " " " " " " "	13%	"	14%,	" " "	26%	" " "
" " " " " " " "	14%	"	15%,	" " "	28%	" " "
" " " " " " " "	15%	"	16%,	" " "	30%	" " "
" " " " " " " "	16%	"	17%,	" " "	32%	" " "
" " " " " " " "	17%	"	18%,	" " "	34%	" " "
" " " " " " " "	18%	"	19%,	" " "	36%	" " "
" " " " " " " "	19%	"	20%,	" " "	38%	" " "

and if the profits amount to more than 20% of the capital, the tax is 40%.

The income tax is general in its character, applying to all profits, gains and incomes exceeding 850 roubles. Limited liability companies are permitted to deduct, in addition to all other provisions concerning deductions, an amount equivalent to 3% of their capital. The rates of the income tax run thus:

On incomes of	10,000	roubles, the tax is	300	roubles	(e. g. 3%)
" " "	15,000	" " " "	600	"	(e. g. 4%)
" " "	20,000	" " " "	1000	"	(e. g. 5%)
" " "	30,000	" " " "	1650	"	(e. g. 5.5%)
" " "	50,000	" " " "	3250	"	(e. g. 6.5%)
" " "	100,000	" " " "	8000	"	(e. g. 8.0%)
" " "	200,000	" " " "	20,000	"	(e. g. 10.0%)
" " "	300,000	" " " "	33,000	"	(e. g. 11%)
" " "	400,000	" " " "	48,000	"	(e. g. 12%)

" " exceeding 40,000 roubles, the tax is 48,000 roubles plus 1250 roubles on each 10,000 roubles exceeding 400,000 roubles.

D. Other Belligerents. It has been impossible to present any reliable data concerning Italy, Austria, Turkey, etc., although no efforts were spared in this direction. Material is exceedingly scant and too old to be of any use at the present moment.

PART V.

War Finance Act

War Finance Act

House of Representatives, 65th Congress, 1st Session. Complete text of the Bond Issue Bill introduced by Representative Kitchin. Approved by President Wilson, April 24, 1917. H. R. 2762.

AN ACT

To authorize an issue of bonds to meet expenditures for the national security and defense, and for the purpose of assisting in the prosecution of the war, to extend credit to foreign governments, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Secretary of the Treasury, with the approval of the President, is hereby authorized to borrow, from time to time, on the credit of the United States for the purposes of this Act, and to meet expenditures authorized for the national security and defense and other public purposes authorized by law not exceeding in the aggregate $5,000,000,000, exclusive of the sums authorized by section four of this Act, and to issue therefor bonds of the United States.

The bonds herein authorized shall be in such form and subject to such terms and conditions of issue, conversion, redemption, maturities, payment, and rate and time of payment of interest, not exceeding three and one-half per centum per annum, as the Secretary of the Treasury may prescribe. The principal and interest thereof shall be payable in United States gold coin of the present standard of value and shall be exempt, both as to principal and interest, from all taxation, except estate or inheritance taxes, imposed by authority of the United States, or its possessions, or by any State or local taxing authority; but such bonds shall not bear the circulation privilege.

The bonds herein authorized shall first be offered at not less than par as a popular loan, under such regulations prescribed by the Secretary of the Treasury as will give all citizens of the United States an equal opportunity to participate therein; and any portion of the bonds so offered and not subscribed for may be otherwise disposed of at not less than par by the Secretary of the Treasury; but no commissions shall be allowed or paid on any bonds issued under authority of this Act.

SEC. 2. That for the purpose of more effectually providing for the national security and defense and prosecuting the war by establishing credits in the United States for foreign governments, the Secretary of the Treasury, with the approval of the President, is hereby authorized, on behalf of the United States, to purchase, at par, from such foreign governments then engaged in war with the enemies of the United States, their obligations hereafter issued, bearing the same rate of interest and containing in their essentials the same terms and conditions as those of the United States issued under authority of this Act; to enter into such arrangements as may be necessary or desirable for establishing such credits and for purchasing such obligations of foreign governments and for the subsequent payment thereof before maturity, but such arrangements shall provide that if any of the bonds of the United States issued and used for the purchase of such foreign obligations shall thereafter be converted into other bonds of the United States bearing a higher rate of interest than three and one-half per centum per annum under the provisions of section five of this Act, then and in that event the obligations of such foreign governments held by the United States shall be, by such foreign governments, converted in like manner and extent into obligations bearing the same rate of interest as the bonds of the United States issued under the provisions of section five of this Act. For the purposes of this section there is appropriated, out of any money in the Treasury not otherwise appropriated, the sum of $3,000,000,000, or so much thereof as may be necessary: *Provided*, That the authority granted by this section to the Secretary of the Treasury to purchase bonds

from foreign governments, as aforesaid, shall cease upon the termination of the war between the United States and the Imperial German Government.

SEC. 3. That the Secretary of the Treasury, under such terms and conditions as he may prescribe, is hereby authorized to receive on or before maturity payment for any obligations of such foreign governments purchased on behalf of the United States, and to sell at not less than the purchase price any of such obligations and to apply the proceeds thereof, and any payments made by foreign governments on account of their said obligations to the redemption or purchase at not more than par and accrued interest of any bonds of the United States issued under authority of this Act; and if such bonds are not available for this purpose the Secretary of the Treasury shall redeem or purchase any other outstanding interest-bearing obligations of the United States which may at such time be subject to call or which may be purchased at not more than par and accrued interest.

SEC. 4. That the Secretary of the Treasury, in his discretion, is hereby authorized to issue the bonds not already issued heretofore authorized by section thirty-nine of the Act approved August fifth, nineteen hundred and nine, entitled "An Act to provide revenue, equalize duties, and encourage the industries of the United States, and for other purposes"; section one hundred and twenty-four of the Act approved June third, nineteen hundred and sixteen, entitled "An Act for making further and more effectual provision for the national defense, and for other purposes"; section thirteen of the Act of September seventh, nineteen hundred and sixteen, entitled "An Act to establish a United States shipping board for the purpose of encouraging, developing, and creating a naval auxiliary and a naval reserve and a merchant marine to meet the requirements of the commerce of the United States with its Territories and possessions and with foreign countries, to regulate carriers by water engaged in the foreign and interstate commerce of the United States, and for other purposes"; section four hundred of the Act approved

March third, nineteen hundred and seventeen, entitled "An Act to provide increased revenue to defray the expenses of the increased appropriations for the Army and Navy and the extensions of fortifications, and for other purposes"; and the public resolution approved March fourth, nineteen hundred and seventeen, entitled, "Joint resolution to expedite the delivery of materials, equipment, and munitions and to secure more expeditious construction of ships," in the manner and under the terms and conditions prescribed in section one of this Act.

That the Secretary of the Treasury is hereby authorized to borrow on the credit of the United States from time to time, in addition to the sum authorized in section one of this Act, such additional amount, not exceeding $63,945,460 as may be necessary to redeem the three per cent. loan of nineteen hundred and eight to nineteen hundred and eighteen, maturing August first, nineteen hundred and eighteen, and to issue therefor bonds of the United States in the manner and under the terms and conditions prescribed in section one of this Act.

SEC. 5. That any series of bonds issued under authority of sections one and four of this Act may, under such terms and conditions as the Secretary of the Treasury may prescribe, be convertible into bonds bearing a higher rate of interest than the rate at which the same were issued if any subsequent series of bonds shall be issued at a higher rate of interest before the termination of the war between the United States and the Imperial German Government, the date of such termination to be fixed by a proclamation of the President of the United States.

SEC. 6. That in addition to the bonds authorized by sections one and four of this Act, the Secretary of the Treasury is authorized to borrow from time to time, on the credit of the United States, for the purposes of this Act and to meet public expenditures authorized by law, such sum or sums as, in his judgment, may be necessary, and to issue therefor certificates of indebtedness at not less than par in such form and subject to such terms and conditions and at such rate of interest, not exceeding three and one-

half per centum per annum, as he may prescribe; and each certificate so issued shall be payable, with the interest accrued thereon, at such time, not exceeding one year from the date of its issue, as the Secretary of the Treasury may prescribe. Certificates of indebtedness herein authorized shall not bear the circulation privilege, and the sum of such certificates outstanding shall at no time exceed in the aggregate $2,000,000,000, and such certificates shall be exempt, both as to principal and interest, from all taxation, except estate or inheritance taxes, imposed by authority of the United States, or its possessions, or by any State or local taxing authority.

SEC. 7. That the Secretary of the Treasury, in his discretion, is hereby authorized to deposit in such banks and trust companies as he may designate the proceeds or any part thereof arising from the sale of the bonds and certificates of indebtedness authorized by this Act, or the bonds previously authorized as described in section four of this Act, and such deposits may bear such rate of interest and be subject to such terms and conditions as the Secretary of the Treasury may prescribe: *Provided*, That the amount so deposited shall not in any case exceed the amount withdrawn from such bank or trust company, and invested in such bonds or certificates of indebtedness plus the amount so invested by such bank or trust company, and such deposits shall be secured in the manner required for other deposits by Section 5153, Revised Statutes, and amendments thereto; *Provided further*, That the provisions of Section 5191 of the Revised Statutes as amended by the Federal Reserve Act and the amendments thereof, with reference to the reserves required to be kept by national banking institutions and other member banks of the Federal Reserve System, shall not apply to deposits of public monies by the United States in designated depositaries.

SEC. 8. That in order to pay all necessary expenses, including rent, connected with any operations under this Act, a sum not exceeding one-tenth of one per centum of the amount of bonds and one-tenth of one per centum of

the amount of certificates of indebtedness herein authorized is hereby appropriated, or as much thereof as may be necessary, out of any money in the Treasury not otherwise appropriated, to be expended as the Secretary of the Treasury may direct: *Provided*, That, in addition to the reports now required by law, the Secretary of the Treasury shall, on the first Monday in December, nineteen hundred and seventeen, and annually thereafter, transmit to the Congress a detailed statement of all expenditures under this Act.

National Bank of Commerce in New York

ORGANIZED 1839

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James S. Alexander

Vice-Presidents

R. G. Hutchins, Jr.
Herbert P. Howell
J. Howard Ardrey
Stevenson E. Ward
John E. Rovensky
Guy Emerson

Cashier
Faris R. Russell

Assistant Cashiers

A. J. Oxenham
William M. St. John
Louis A. Keidel
A. F. Maxwell
John J. Keenan
Gaston L. Ghegan
A. F. Broderick
Everett E. Risley
H. P. Barrand

Auditor
Richard W. Saunders

Manager Foreign Department
Franz Meyer

Statement of Condition

May 1, 1917

RESOURCES

Loans and Discounts	$213,573,592.25
Bonds, Securities, etc.	32,203,265.01
Banking House	2,000,000.00
Due from Banks and Bankers	32,378,420.92
Cash, Exchanges and due from Federal Reserve Bank	103,069,036.72
Customers' Liability under Letters of Credit, Acceptances, etc.	29,590,321.58
Interest Accrued	704,794.53
	$413,519,431.01

LIABILITIES

Capital, Surplus and Undivided Profits	$ 44,850,500.65
Deposits	338,068,215.86
National Bank Notes outstanding	155,000.00
Letters of Credit and Acceptances	26,912,426.24
Unearned Discount	790,516.86
Other Liabilities	2,742,771.40
	$413,519,431.01

PUBLICATIONS

The following recent publications of the National Bank of Commerce in New York are still available for distribution to persons interested:

EXCESS PROFITS TAX LAW—Official Text with Relating Sections of the Income Tax Law, March 3, 1917.

THE VIRGIN ISLANDS—A Description of the Commercial Value of the Danish West Indies, April, 1917.

SAVING AMERICA FROM BANKRUPTCY—An Intimate Story of the First Civil War Loan, by Edith Vail Taylor, April, 1917.

GOLD—A Study of the Shifting of the Golden Basis of Credit from Belligerents to Neutrals and the Dangers in the Situation, by J. E. Rovensky, April, 1917.

THE PRINCIPLES INVOLVED IN WAR FINANCING—By James S. Alexander, May, 1917.

WAR FINANCE PRIMER, May, 1917.

SERVICE DEPARTMENT

National Bank of Commerce in New York

NATIONAL BANK OF COMMERCE
1839
IN NEW YORK